

**The Statewide Single Audit of the Commonwealth of Kentucky
For the Year Ended June 30, 2004**

BACKGROUND

The Single Audit Act of 1984, subsequent amendments, and corresponding regulations, require the auditing of financial statements and the compliance and internal controls applicable to federal moneys received by the Commonwealth.

STATE AGENCIES EXPENDED MORE FEDERAL AWARDS IN FY 04

Total federal expenditures increased by \$472,801,910 in FY 04. State organizations expended \$6,997,120,187 in federal awards in FY 04; whereas, state organizations expended \$6,524,318,277 in federal awards in FY 03.

FINDINGS IN FY 04

There were 9 more findings in FY 04, than in FY 03. There were 49 findings for FY 04; whereas there were 40 findings in FY 03. Of the 49 findings for FY 04, 17 were related to the financial statements, and 32 were related to federal awards. We qualified the OMB Circular A-133 compliance opinion for CFDA 97.004 and CFDA 97.036.

NEW FINDINGS FOR FY 04

Cabinet for Families and Children

- Processing of Unemployment Insurance Claimant Overpayments
- Maintenance of Case Files Records
- Payments Made to Eligible Recipients are Approved and Allowable
- Eligibility for Work Incentive Payments
- Reporting and Spending of Unliquidated Balances
- Child Support Enforcement Performance

Cabinet for Health Services

- Better Safeguards for Funds
- Subrecipient Monitoring

Cabinet for Workforce Development

- Proper Review of Timesheets, Department for Employment Services
- Allowable Costs, Department for Employment Services
- Strengthen Controls to Ensure Compliance with Federal Earmarking Requirements, Department for Employment Services
- Timely Journal Voucher Processing, Department for Training and ReEmployment

Department of Fish and Wildlife Resources

- Proper Timesheet Approval
- Consider Requesting General Assembly to Adopt 50 CFR 80.3-80.4 into State Law
- Proper Recording of Program Income

Department of Military Affairs

- Procedures to comply with NGR 5-1/ANGI 63-101 Relating To Program Income For The National Guard Program
- Controls for Retaining Support for PX Documents

**The Statewide Single Audit of the Commonwealth of Kentucky
For the Year Ended June 30, 2004
(Continued)**

Department of Military Affairs

- Controls for Compliance with Federal Program Requirements
- Monitor Grant Supported Activities to Assure Compliance with Applicable Federal Requirements

Department of Parks

Controls over Timesheets and payroll reports

Department of Revenue

- Accurate Processing of Sales and Use Tax Returns
- Sales and Use Tax Returns Reconciled Monthly
- Adequate testing of System Changes

Finance and Administration Cabinet

- Procedures to Ensure Accuracy of Year End Investment Income Accrual, Office of Financial Management
- Logical Security Procedures Surrounding Complete Assets Management Reporting and Accounting System

Justice Cabinet

- Monitor Grant Funds Passed-Thru To Other State Agencies For Compliance With Grant Requirements
- Procedures To Ensure All Grant Funds Are Expended In Accordance With Federal Guidelines
- Supplanting State Funds with Federal Funds

Natural Resources and Environmental Protection Cabinet

- Subrecipient Monitoring

Transportation Cabinet

- Improve The Change Order Process
- Improve Procedures To Ensure Federal Reports Are Submitted Timely
- Improve Procedures To Ensure Federal Reports Are Prepared Accurately
- Improve Review And Authorization Procedures For Relocation Payments
- Ensure FHWA Approval Is Obtained Before Relocation Payments Are Made
- Inventory Procedures for Maintenance Materials
- Procedures to Ensure Accurate Conversion of Data to New Systems
- Audit Trail Procedures for Database Actions

**The Statewide Single Audit of the Commonwealth of Kentucky
For the Year Ended June 30, 2004
(Continued)**

STATE AGENCIES WITH RECURRING FINDINGS

Cabinet for Families and Children

- Password Security
- Local Area Network Server Security
- Support for Expenditures

Cabinet for Workforce Development

- Closing Package Reporting, Division of Unemployment Insurance
- Adequate Maintenance of Employer Accounts, Division of Unemployment Insurance
- Accurate Federal Reporting, Department for Training and ReEmployment

Department of Military Affairs

- Subrecipient Monitoring

Finance and Administration Cabinet

- Control Procedures over Modifications to System Programs
- Procedures for the Cash and Investment Statistical Analysis System Programs
- Accurate and Timely Fixed Asset Counts for all State Agencies
- Segregation of Duties, Office of Financial Management
- Policies and Procedures to Govern Security of the Management Administrative and Reporting System

Justice Cabinet

- Indirect Cost Plan Submission to Cognizant Federal Agency
- Subrecipient Monitoring
- Quarterly Status Report and Supporting Documentation

Transportation Cabinet

- Procedures to Ensure Accurate Presentation of Federal Highway Administration Statistics Report
- Federal Guideline Compliance for the Federal Highway Administration Statistics Report
- Federal Highway Administration Approvals Prior to Advertising for Projects
- Procedures to Ensure the Integrity of the Highway Information System Database
- Data Retention Practices

**STATE AGENCIES WITH UNRESOLVED FEDERAL AWARD
QUESTIONED COSTS IN FY 04**

Cabinet for Families and Children	\$ 36,038 (FY 04)
Cabinet for Families and Children	\$ 5,791 (FY 03)
Department of Military Affairs	\$ 98,679 (FY 04)
Justice Cabinet	\$393,864 (FY 04)
Justice Cabinet	\$ 46,774 (FY 03)
Transportation Cabinet	\$ 65,129 (FY 04)



CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

March 24, 2005

Honorable Ernie Fletcher, Governor
Cabinet Secretaries and Agency Heads
Members of the Commonwealth of Kentucky Legislature

As Auditor of Public Accounts, I am pleased to transmit herewith our report of the Statewide Single Audit of the Commonwealth of Kentucky for the year ended June 30, 2004. The Federal Government's Office of Management and Budget (OMB), per OMB Circular A-133 requires the Auditor of Public Accounts to perform the Statewide Single Audit of the Commonwealth of Kentucky.

To fulfill these requirements, the Auditor of Public Accounts, performs the following:

- An audit of the basic financial statements and combining and individual fund statements and schedules-nonmajor funds;
- Limited procedures applied to required supplementary information;
- An audit of the Schedule of Expenditures of Federal Awards;
- An audit of compliance with the compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* applicable to each major federal program;
- Tests of internal control over compliance in accordance with OMB Circular A-133;
- Tests of compliance with certain provisions of laws, regulations, contracts, and grants; and
- Tests of internal control over financial reporting.

The Auditor of Public Accounts also calculates a dollar threshold, based on OMB Circular A-133 guidance, to determine the federal programs to be audited for internal controls and compliance. For FY 04, the threshold for auditing federal programs was \$20 million.

On behalf of the Division of Financial Audit of the Auditor of Public Accounts' Office, I wish to thank the employees of the Commonwealth for their cooperation during the course of our audit. Should you have any questions concerning this report, please contact John Cubine, Director, Division of Financial Audit, or me.

Respectfully submitted,

A handwritten signature in cursive script, reading "Crit Luallen".

Crit Luallen
Auditor of Public Accounts



**REPORT OF THE
STATEWIDE SINGLE AUDIT OF THE
COMMONWEALTH OF KENTUCKY**

**For The Year Ended
June 30, 2004**



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INTRODUCTION

**COMMONWEALTH OF KENTUCKY
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2004**

Single Audit Report

The Auditor of Public Accounts (APA), acting as principal auditor in conjunction with various certified public accounting firms, annually performs a statewide single audit of the Commonwealth of Kentucky.

The APA prepares the Single Audit Report in compliance with Government Auditing Standards, Generally Accepted Government Auditing Standards, and the requirements of Office of Management and Budget (OMB) Circular A-133. The APA, on behalf of the Commonwealth of Kentucky, also prepares a reporting package as required by OMB Circular A-133. The reporting package includes the basic financial statements, Schedule of Expenditures of Federal Awards (SEFA), auditor's reports, Summary Schedule of Prior Audit Findings, and corrective action plans. For the fiscal year ended June 30, 2004 (FY 04), the Single Audit Report is presented in two reports: the Comprehensive Annual Financial Report (CAFR) and the Single Audit Report.

The CAFR, which contains the basic financial statements and the auditor's report thereon, has been issued under separate cover.

The Single Audit Report contains the auditor's reports on internal control over financial reporting and on compliance and other matters, compliance and internal control over compliance with requirements applicable to major federal programs, and the supplementary SEFA. The Single Audit Report also contains the SEFA, Schedule of Findings and Questioned Costs, and the Summary Schedule of Prior Audit Findings.

Schedule of Expenditures of Federal Awards

The SEFA is organized by federal grantor. The Catalog of Federal Domestic Assistance (CFDA) numbers and program names are listed under the federal grantor administering the program. The state organizations expending the federal funds are listed beside each CFDA number. The notes to the SEFA provide more detailed information on certain aspects of the expenditures. Clusters of programs are indicated in the schedule by light gray shading.

Schedule of Findings and Questioned Costs

The Schedule of Findings and Questioned Costs consists of three (3) sections: Summary of Auditor's Results, Financial Statement Findings, and Federal Award Findings and Questioned Costs. The Summary of Auditor's Results summarizes the type of audit reports issued and lists major programs audited. The Financial Statement Findings list the audit findings related to the financial statements. The Federal Award Findings and Questioned Costs lists all findings related to federal awards. In both sections, reportable conditions and reportable instances of noncompliance are presented first, then material weaknesses and material instances of noncompliance.

**COMMONWEALTH OF KENTUCKY
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Summary Schedule of Prior Audit Findings

Audit findings reported in the Schedule of Findings and Questioned Costs for FY 03, as well as any previous findings that have not been resolved, are reported in the Summary Schedule of Prior Audit Findings for FY 04.

The Summary Schedule of Prior Audit Findings is organized based on whether the prior year finding was reportable or material. The findings of each classification (reportable and material) are categorized as (1) fully corrected, (2) not corrected or partially corrected, (3) corrective action taken differs significantly from corrective action previously reported, or (4) finding no longer valid or does not warrant further action.

Audit Approach

The scope of the statewide single audit for FY 04 included:

- An audit of the basic financial statements and combining and individual fund statements and schedules-nonmajor funds;
- Limited procedures applied to required supplementary information;
- An audit of the SEFA;
- An audit of compliance with the compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* applicable to each major federal program;
- Tests of internal control over compliance in accordance with OMB Circular A-133;
- Tests of compliance with certain provisions of laws, regulations, contracts, and grants; and
- Tests of internal control over financial reporting.

Status of State Universities

The Single Audit Act Amendments permit the single audit to cover the entire operations of the entity or include a series of audits covering departments, agencies, or other organizational units expending federal awards. The agencies audited as part of the Statewide Single Audit of the Commonwealth of Kentucky are listed in Appendix 1. The Commonwealth has elected to exclude state universities from the statewide single audit, except as part of the audit of the basic financial statements. Thus, state universities are not included in the accompanying Schedule of Expenditures of Federal Awards and reports on internal control and compliance. It should be noted, however, that state universities are still required to have audits performed in accordance with the provisions of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

**COMMONWEALTH OF KENTUCKY
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

List Of Abbreviations/Acronyms Used In This Report

ABC	Department of Alcoholic Beverage Control
AGR	Department of Agriculture
AMLR	Abandoned Mine Land Reclamation
AOC	Administrative Office of the Courts
AYOM	MARS Program Budget Unit
BMS	Bridge Maintenance System
BDC	Backup Domain Controller
BOE	Board of Elections
CAP	Cost Allocation Plan
CCSHCN	Commission for Children with Special Health Care Needs
CFC	Cabinet for Families and Children
CFDA	Catalog of Federal Domestic Assistance
CFR	Code of Federal Regulations
CHFS	Cabinet for Health and Family Services
CHS	Cabinet for Health Services
CMS	Center for Medicare and Medicaid Services
CORR	Department of Corrections
COT	Commonwealth Office of Technology
CPE	Council on Postsecondary Education
CR	Cash Receipt Document
CVC	Crime Victims Compensation Board
CWD	Cabinet for Workforce Development
DAEL	Department of Adult Education and Literacy
DCBS	Department of Community Based Services
DCD	Department for Community Development
DCJT	Department of Criminal Justice Training
DFWR	Department of Fish & Wildlife Resources
DHHS	Department of Health and Human Services
DLA	Department for Libraries and Archives
DLG	Department for Local Government
DMA	Department of Military Affairs
DMS	Department of Medicaid Services
DOL	Department of Labor
DPH	Department for Public Health
DTR	Department of Training and ReEmployment
DVA	Department of Veterans Affairs
ECOS	Electronic Commodity Ordering System
EDU	Department of Education
EMSB	Emergency Medical Standards Board
EPSB	Education Professional Standards Board

**COMMONWEALTH OF KENTUCKY
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

List Of Abbreviations/Acronyms Used In This Report (Continued)

EPA	Environmental Protection Agency
F&W	Department of Fish and Wildlife Resources
FAC	Finance and Administration Cabinet
FHWA	Federal Highway Administration
FMO	Facilities Management Officer
FSM	Family Support Memorandums
FSR	Financial Status Report
FTA	Federal Transit Administration
GAAP	Generally Accepted Accounting Principles
GMB	Grants Management Branch
GOV	Office of the Governor
GPO	Group Policy Objects
HBC	Housing Buildings and Construction
HIDTA	High Intensity Drug Trafficking Area
HIS	Highway Information System
HRC	Kentucky Commission on Human Rights
IAW	In Accordance With
ID	Identification
IDCRP	Indirect Cost Rate Proposal
IMF	Installation Management Fund
IT	Information Technology
JUST	Justice Cabinet
JUV	Department of Juvenile Justice
JV	Journal Voucher
JVB	Journal Voucher
KAC	Kentucky Arts Council
KAMES	Kentucky Automated Management and Eligibility System
KAR	Kentucky Administrative Regulation
KBIS	Kentucky Bridge Information System
KCA	Kentucky Center for the Arts
KDVA	Kentucky Department of Veterans Affairs
KET	Kentucky Educational Television
KHC	Kentucky Heritage Council
KHCORP	Kentucky Housing Corporation
KHEAA	Kentucky Higher Education Assistance Authority
KHESLC	Kentucky Higher Education Student Loan Corporation
KHS	Kentucky Historical Society
KIA	Kentucky Infrastructure Authority
KRS	Kentucky Revised Statutes
KSP	Kentucky State Police

**COMMONWEALTH OF KENTUCKY
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

List Of Abbreviations/Acronyms Used In This Report (Continued)

KyBMS	Kentucky Bridge Maintenance System
KyDEM	Kentucky Department of Emergency Management
K-TAP	Kentucky Transitional Assistance Program
KWP	Kentucky Works Program
LAB	Labor Cabinet
LHD	Local Health Departments
LWIA	Local Workforce Investment Areas
M&M	Department of Mines and Minerals
MARS	Management Administrative Reporting System
MOA	Memorandum of Agreement
NA	Not Applicable
NBIS	National Bridge Information System
NCGA	National Council of Governmental Accounting
NEG	National Emergency Grant
NREPC	Natural Resources and Environmental Protection
NT	New Technology
OAG	Office of the Attorney General
OET	Office of Employment Training
OFM	Office of Financial Management
OIG	Office of Inspector General
OMB	Office of Management and Budget
OMS	Operations Management System
OMTL	Operations Manual Transmittal Letter
OMU	Operations Manual Updates
PARKS	Department of Parks
PCR	Program Change Request
PDC	Primary Domain Controller
PMS	Pavement Management System
PSC	Public Service Commission
PUBAD	Department of Public Advocacy
R&D	Research and Development
REV	Department of Revenue
Revenue	Department of Revenue
SCG	State Cemetery Grants
SMI	Supplementary Medical Insurance
SOLQ	State On-Line Query System
SQL	Structured Query Language
SSN	Social Security Number
TANF	Temporary Assistance for Needy Families
TC	Transportation Cabinet

**COMMONWEALTH OF KENTUCKY
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

List Of Abbreviations/Acronyms Used In This Report (Continued)

TSC	Training Centers
UI	Unemployment Insurance
UPPS	Uniform Payroll and Personnel System
UPS	Unified Prosecutorial System
US	United States
USDA	United States Department of Agriculture
USDOJ	United States Department of Justice
UTES/MATES/AASF	Types of Building Codes
VA	Department of Veterans' Affairs
VAWA	Violence Against Women Formula Grants
VOCA	Crime Victim Assistance Grant
WIN	Work Initiative
W/P	Wagner-Peyser Act

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
U.S. Office of National Drug Control Policy					
Direct Program:					
07.NA(1)	HIDTA Program	KSP	\$	781,765	
Total U.S. Office of National Drug Control Policy			\$	781,765	
U.S. Department of Agriculture					
Direct Programs:					
10.025	Plant and Animal Disease, Pest Control, and Animal Care	AGR	\$	409,662	\$
		F&W		52,731	
10.028	Wildlife Services (Note 9)	F&W		40,649	
10.069	Conservation Reserve Program (Note 14)	NREPC		12,034	
		F&W			
10.153	Market News	AGR		2,519	
10.156	Federal- State Marketing Improvement Program	AGR		48,935	
10.163	Market Protection and Promotion	AGR		61,623	
10.550	Food Donation (Note 13)	AGR			18,078,056
		CORR			179,522
Food Stamp Cluster:					
10.551	Food Stamps (Note 2) (Note 13)	CFC			533,396,719
10.561	State Administrative Matching Grants for Food Stamp Program (Note 2)	CFC		27,381,977	740,816
		OAG		325,784	
		CHS		113,846	
Child Nutrition Cluster:					
10.553	School Breakfast Program (Note 2)	EDU		35,722,444	35,645,044
		JUV		300,379	
10.555	National School Lunch Program (Note 2)	EDU		110,190,526	110,036,154
		JUV		481,282	
10.556	Special Milk Program for Children (Note 2)	EDU		88,468	88,468
10.559	Summer Food Service Program for Children (Note 2)	EDU		6,154,494	5,984,062
10.557	Special Supplemental Nutrition Program for Women, Infants, and Children (Note 2)	CHS		88,002,978	15,927,294
10.558	Child and Adult Care Food Program (Note 2)	EDU		24,372,132	23,885,750
10.560	State Administrative Expenses for Child Nutrition	EDU		2,368,647	
		AGR		204,963	
10.565	Commodity Supplemental Food Program (Note 4) (Note 13)	AGR		1,039,472	3,096,139
Emergency Food Assistance Cluster:					
10.568	Emergency Food Assistance Program (Administrative Costs)	AGR		833,294	
10.569	Emergency Food Assistance Program (Food Commodities) (Note 13)	AGR			5,740,332

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Department of Agriculture (Continued)</u>					
Direct Programs (Continued):					
10.572	WIC Farmers' Market Nutrition Program (FMNP)	AGR	\$ 140,315		
10.576	Senior Farmers Market Nutrition Program	AGR	276,403		
10.652	Forestry Research	NREPC	313,255		
10.664	Cooperative Forestry Assistance (Note 13)	NREPC	2,523,631	572,027	455,265
10.672	Rural Development, Forestry, and Communities	NREPC	104,674		
10.766	Community Facilities Loans and Grants (Note 2) (Note 3e) (Note 13)	KHCORP		69,333,397	
10.771	Rural Cooperative Development Grants (Note 14)	AGR			
10.861	Public Television Station Digital Transition Grant (Note 14)	KET			
10.902	Soil and Water Conservation	NREPC	666,801		
		F&W	134,527		
10.912	Environmental Quality Incentives Program	NREPC	191		
10.914	Wildlife Habitat Incentive Program (Note 13)	F&W		5,250	
10.NA(1)	Rural Rehabilitation Student Loan Program (Note 3a)	AGR	111,383		
Total U.S. Department of Agriculture			<u>\$ 302,480,019</u>	<u>\$ 630,401,442</u>	<u>\$ 192,762,853</u>
<u>U.S. Department of Commerce</u>					
Direct Programs:					
Public Works and Economic Development Cluster:					
11.307	Economic Adjustment Assistance (Note 3b) (Note 14)	DLG	\$		
11.450	Automated Flood Warning Systems (AFWS)	MIL	54,014		
11.550	Public Telecommunications Facilities Planning and Construction (Note 2)	KET	807,505		
Total U.S. Department of Commerce			<u>\$ 861,519</u>		
<u>U.S. Department of Defense</u>					
Direct Programs:					
12.002	Procurement Technical Assistance For Business Firms	DCD	\$ 130,182		\$
12.113	State Memorandum of Agreement Program for the Reimbursement of Technical Services	NREPC	364,493		
12.400	Military Construction, National Guard	MIL	245,684		
12.401	National Guard Military Operations and Maintenance (O & M) Projects	MIL	10,816,969		
12.404	National Guard Civilian Youth Opportunities	MIL	1,790,996		
12.NA(1)	Chemical Demilitarization and Remediation Activity for Hazardous Waste Activities at Chemical Demilitarization Facilities	NREPC	49,446		9,214
12.NA(2)	Monitoring of Wildlife	F&W	10,765		
12.NA(3)	Teacher and Teacher's Aide Placement Assistance Program	EPSB	40,427		
Total U.S. Department of Defense			<u>\$ 13,448,962</u>	<u>\$</u>	<u>9,214</u>

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Department of Housing and Urban Development</u>					
Direct Programs:					
14.117	Mortgage Insurance - Homes (Note 2) (Note 3e) (Note 13)	KHCORP	\$	\$ 124,331,475	\$
14.169	Housing Counseling Assistance Program	KHCORP		141,896	
Section 8 Project-Based Cluster:					
14.182	Lower Income Housing Assistance Program-Section 8 New Construction/Substantial Rehabilitation (Note 2)	KHCORP		84,425,207	
14.856	Lower Income Housing Assistance Program-Section 8 Moderate Rehabilitation (Note 2)	KHCORP		87,934	
14.228	Community Development Block Grants/State's Program (Note 2) (Note 10)	DLG HRC	31,037,919 103		30,525,826
14.231	Emergency Shelter Grants Program	KHCORP	1,333,425		1,290,157
14.235	Supportive Housing Program (Note 2)	KHCORP	3,511,592		3,489,659
14.238	Shelter Plus Care	KHCORP	353,030		242,422
14.239	HOME Investment Partnerships Program	KHCORP	18,850,546		10,028,941
14.241	Housing Opportunities for Persons with AIDS	KHCORP	677,002		654,973
14.401	Fair Housing Assistance Program-State and Local	HRC	297,860		
14.408	Fair Housing Initiatives Program (Note 14)	HRC			
14.409	Fair Housing Initiatives Program (FHIP) Education and Outreach Initiative	HRC	19,428		
14.871	Section 8 Housing Choice Vouchers (Note 2)	KHCORP	22,851,045		
14.NA(1)	HUD Disaster Recovery Initiative	DLG	164,521		164,521
Total U.S. Department of Housing and Urban Development			\$ 163,751,508	\$ 124,331,475	\$ 46,396,499
<u>U.S. Department of the Interior</u>					
Direct Programs:					
15.250	Regulation of Surface Coal Mining and Surface Effects of Underground Coal Mining (Note 13)	NREPC	\$ 12,393,931	\$ 35,802	\$
15.252	Abandoned Mine Land Reclamation (AMLR) Program (Note 2)	NREPC	23,370,703		5,346,529
Fish and Wildlife Cluster:					
15.605	Sport Fish Restoration (Note 9)	F&W	4,074,800		
15.611	Wildlife Restoration (Note 11)	F&W	3,881,466		
15.608	Fish and Wildlife Management Assistance	NREPC	2,926		
15.615	Cooperative Endangered Species Conservation Fund (Note 9)	F&W NREPC	183,076 25,866		
15.616	Clean Vessel Act	F&W	34,164		
15.618	Administrative Grants for Federal Aid in Sport Fish and Wildlife Restoration (Note 14)	F&W			
15.622	Sportfishing and Boating Safety Act	F&W	98,950		

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Department of the Interior (Continued)</u>					
Direct Programs (Continued):					
15.623	North American Wetlands Conservation Fund (Note 14)	NREPC			
15.625	Wildlife Conservation and Restoration (Note 9)	F&W	50,299		
15.632	Conservation Grants Private Stewardship for Imperiled Species	F&W	26,029		
15.633	Landowner Incentive	F&W	531,860		489,076
15.634	State Wildlife Grants (Note 9)	F&W	440,486		
15.808	U.S. Geological Survey-Research and Data Collector (Note 13)	NREPC		58,500	
		F&W	19,718		
15.904	Historic Preservation Fund Grants-In-Aid	KHC	537,694		51,250
15.916	Outdoor Recreation-Acquisition, Development and Planning (Note 7)	DLG	1,154,361		1,154,361
		PARKS	9,821		
15.NA(1)	Federal Junior Duck Stamp Conservation and Design	F&W	2,155		
15.NA(2)	National Fish and Wildlife Foundation-Restoration of Elk Habitat in Kentucky	F&W	6,046		
Total U.S. Department of the Interior			\$ 46,844,351	\$ 94,302	\$ 7,041,216
<u>U.S. Department of Justice</u>					
Direct Programs:					
16.523	Juvenile Accountability Incentive Block Grants	JUV	\$ 2,576,064		\$ 1,738,766
		PUBAD	73,131		
		UPS	70,997		
		AOC	59,170		
16.540	Juvenile Justice and Delinquency Prevention-Allocation to States	JUV	1,082,408		1,055,110
16.541	Developing, Testing and Demonstrating Promising New Programs	AOC	7,265		
16.543	Missing Children's Assistance	KSP	201,288		
16.548	Title V-Delinquency Prevention Program	JUV	266,315		254,902
16.549	Part E-State Challenge Activities	JUV	69,168		69,168
16.550	State Justice Statistics Program for Statistical Analysis Centers	JUST	49,797		
16.554	National Criminal History Improvement Program (NCHIP) (Note 14)	KSP	980,495		
		JUST			
16.560	National Institute of Justice Research, Evaluation, and Development Project Grants	JUST	24,163		
		KSP	21,496		
16.564	Crime Laboratory Improvement-Combined Offender DNA Index System Backlog Reduction	KSP	134,402		
16.575	Crime Victim Assistance	JUST	4,427,349		4,260,462
		UPS	478,022		
16.576	Crime Victim Compensation	CVC	198,604		

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Department of Justice (Continued)</u>					
Direct Programs (Continued):					
16.579	Byrne Formula Grant Program (Note 9)	JUST	3,154,233		2,592,362
		KSP	1,816,004		
		AOC	1,221,551		44,018
		JUV	80,604		80,604
		PUBAD	67,669		
		UPS	15,590		
		OAG	7,655		7,653
		CORR	7,452		
16.580	Edward Byrne Memorial State and Local Law Enforcement Assistance Discretionary Grants Program (Note 14)	AOC	742,330		
		JUST			
		CFC			
16.585	Drug Court Discretionary Grant Program (Note 9)	AOC	869,736		
16.586	Violent Offender Incarceration and Truth in Sentencing Incentive Grants	CORR	4,210,697		
		JUV	2,559,500		43,233
		JUST	14,489		
16.588	Violence Against Women Formula Grants	JUST	1,675,859		1,626,560
		UPS	205,784		
		OAG	64,628		
		GOV	10,000		
		AOC	3,500		
16.589	Rural Domestic Violence and Child Victimization Enforcement Grant Program	JUST	113,838		113,838
16.592	Local Law Enforcement Block Grants Program	JUST	423,106		417,504
		KSP	397,365		
16.593	Residential Substance Abuse Treatment for State Prisoners (Note 14)	CORR	803,944		
		JUST			
16.606	State Criminal Alien Assistance Program	CORR	13,249		
16.607	Bulletproof Vest Partnership Program (Note 14)	JUST			
		KSP			
16.609	Community Prosecution and Project Safe Neighborhoods	UPS	158,006		
16.710	Public Safety Partnership and Community Policing Grants (Note 12) (Note 14)	KSP	533,209		
		JUST			
16.712	Police Corps	DCJT	1,453,636		
16.727	Enforcing Underage Drinking Laws Program	KSP	178,830		116,621
		ABC	155,000		
16.728	Drug Prevention Program	TC	38,756		
16.NA(1)	Drug Enforcement Administration	KSP	804,732		
16.NA(2)	Federal Bureau of Investigation	KSP	28,414		
16.NA(3)	Federal Methamphetamine Initiative	KSP	50,956		

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Department of Justice (Continued)</u>					
Passed Through From Eastern Kentucky University:					
16.710	Public Safety Partnership and Community Policing Grants Pass Through Grantor's #-97-CK-WK-1 (Note 12) (Note 14)	DCJT			
Total U.S. Department of Justice			\$ 32,600,456		\$ 12,420,801
<u>U.S. Department of Labor</u>					
Direct Programs:					
17.002	Labor Force Statistics	CWD	\$ 1,000,144		\$
17.005	Compensation and Working Conditions	LAB	117,715		
17.203	Labor Certification for Alien Workers	CWD	389,791		
Employment Services Cluster:					
17.207	Employment Service	CWD	10,570,861		1,746
17.801	Disabled Veterans' Outreach Program (DVOP)	CWD	797,405		
17.804	Local Veterans' Employment Representative Program	CWD	1,059,249		
17.225	Unemployment Insurance (Note 2) (Note 5)	CWD	563,143,624		34,555
17.235	Senior Community Service Employment Program	CHS	1,641,946		1,594,277
17.245	Trade Adjustment Assistance-Workers (Note 2)	CWD	21,569,133		
17.253	Welfare-to-Work Grants to States and Localities (Note 14)	CFC			
Workforce Investment Act Cluster:					
17.258	WIA Adult Program (Note 2)	CWD	14,659,945		13,776,202
		EDU	1,035,266		945,874
17.259	WIA Youth Activities (Note 2)	CWD	13,446,328		12,958,719
		MIL	294,442		
17.260	WIA Dislocated Workers (Note 2)	CWD	15,229,340		12,902,762
17.263	Youth Opportunity Grants	CWD	143,077		129,090
17.267	WIA Incentive Grants-Section 503 Grants to States (Note 2)	CWD	1,196,774		1,209,180
		CPE	808,367		
		MIL	298,105		
17.503	Occupational Safety and Health-State Program	LAB	3,403,576		
17.504	Consultation Agreements	LAB	24,763		
17.600	Mine Health and Safety Grants	M&M	503,020		
17.601	Mine Health and Safety Counseling and Technical Assistance	M&M	167,627		
Total U.S. Department of Labor			\$ 651,500,498		\$ 43,552,405

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
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CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Department of Transportation</u>					
Direct Programs:					
Highway Planning and Construction Cluster:					
20.205	Highway Planning and Construction (Note 2) (Note 6) (Note 14)	TC PARKS KSP NREPC	\$ 466,540,160 123,213 8,697		\$ 392,925
20.218	National Motor Carrier Safety	TC KSP	3,954,629 191,440		52,531
20.219	Recreational Trails Program (Note 7) (Note 14)	DLG PARKS	788,673		706,872
20.505	Federal Transit-Metropolitan Planning Grants	TC	366,412		312,430
Federal Transit Cluster:					
20.500	Federal Transit-Capital Investment Grants	TC	14,280,733		14,280,733
20.509	Formula Grants for Other Than Urbanized Areas	TC	7,250,998		6,658,742
20.513	Capital Assistance Program for Elderly Persons and Persons with Disabilities	TC	1,744,495		1,719,495
Highway Safety Cluster:					
20.600	State and Community Highway Safety (Note 14)	KSP DCJT	3,936,879		1,508,103
20.604	Safety Incentive Grants for Use of Seatbelts	KSP	616,884		374,426
20.605	Safety Incentives to Prevent Operation of Motor Vehicles by Intoxicated Persons	KSP	11,014		
20.700	Pipeline Safety	PSC	239,365		
20.703	Interagency Hazardous Materials Public Sector Training and Planning Grants	MIL	172,467		
Total U.S. Department of Transportation			\$ 500,226,059		\$ 26,006,257
<u>U.S. Department of Treasury</u>					
Direct Programs:					
21.NA(1)	Internal Revenue Service	KSP	\$ 2,450		
21.NA(2)	Job Growth Tax Relief Reconciliation Act (Note 2)	FAC	68,720,606		
Total U.S. Department of Treasury			\$ 68,723,056		
<u>U.S. Appalachian Regional Commission</u>					
Direct Programs:					
23.001	Appalachian Regional Development	DLG	\$ 82,031		\$
23.002	Appalachian Area Development	DLG KHCORP	597,604 549,759		597,604

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Appalachian Regional Commission (Continued)</u>					
Direct Programs (Continued);					
23.011	Appalachian State Research, Technical Assistance, and Demonstration Projects	DLG FAC PARKS	471,009 103,960 68,431		470,411 103,960
23.NA(1)	Kentucky Appalachian Motorcoach Tourism Planning Grant (Note 14)	TRAV			
Total U.S. Appalachian Regional Commission			\$ 1,872,794		\$ 1,171,975
<u>U.S. Equal Employment Opportunity Commission</u>					
Direct Programs:					
30.002	Employment Discrimination-State and Local Fair Employment Practices Agency Contracts	HRC	\$ 129,547		
Total U.S. Equal Employment Opportunity Commission			\$ 129,547		
<u>U.S. General Services Administration</u>					
Direct Programs:					
39.003	Donation of Federal Surplus Personal Property (Note 13)	FAC	\$	\$ 627,599	\$
39.011	Election Reform Payments (Note 9)	BOE	314,850		239,416
Total U.S. General Services Administration			\$ 314,850	\$ 627,599	\$ 239,416
<u>U.S. National Aeronautics and Space Administration</u>					
Direct Program:					
43.NA(1)	Kentucky Landscape Snapshot (Note 13)	NREPC		\$ 10,985	
Total U.S. National Aeronautics and Space Administration				\$ 10,985	
<u>U.S. National Foundation on the Arts and the Humanities</u>					
Direct Programs:					
45.024	Promotion of the Arts-Grants to Organizations and Individuals	KCA KET	\$ 23,250 19,154		\$
45.025	Promotion of the Arts-Partnership Agreements	KAC KCA KHS	528,416 33,100 20,000		283,812
45.026	Promotion of the Arts-Leadership Initiatives (Note 14)	KHS KAC	14,721		

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. National Foundation on the Arts and the Humanities (Continued)</u>					
Direct Programs (Continued):					
45.129	Promotion of the Humanities-Federal/State Partnership (Note 14)	KHS			
45.149	Promotion of the Humanities-Division of Preservation and Access	KHS	17,200		
45.310	State Library Program	DLA	2,362,482		753,712
Total U.S. National Foundation on the Arts and Humanities			\$ 3,018,323		\$ 1,037,524
<u>U.S. Department of Veterans Affairs</u>					
Direct Programs:					
64.005	Grants to States for Construction of State Home Facilities:	VA	\$ 2,040,905	\$	
64.114	Veterans Housing-Guaranteed and Insured Loans (Note 2) (Note 3e) (Note 13)	KHCORP		9,042,601	
64.203	State Cemetery Grants	VA	2,886,239		
Total U.S. Department of Veterans Affairs			\$ 4,927,144	\$ 9,042,601	
<u>U.S. Environmental Protection Agency</u>					
Direct Programs:					
66.001	Air Pollution Control Program Support	NREPC	\$ 1,643,013	\$	\$
66.032	State Indoor Radon Grants	CHS	481,438		330,923
66.419	Water Pollution Control State and Interstate Program Support	NREPC	1,844,080		29,925
66.432	State Public Water System Supervision	NREPC	833,700		
66.438	Construction Management Assistance	NREPC	335,770		
66.454	Water Quality Management Planning	NREPC	234,594		15,000
66.458	Capitalization Grants for Clean Water State Revolving Funds (Note 2) (Note 3d)	KIA	8,203,334		7,992,287
		NREPC	322,564		
66.460	Nonpoint Source Implementation Grants	NREPC	3,434,803		1,028,136
66.461	Wetland Program Grants	NREPC	242,128		
		F&W	79,692		
66.463	Water Quality Cooperative Agreements	NREPC	45,851		40,644
66.467	Wastewater Operator Training Grant Program (Technical Assistance)	NREPC	35,143		
66.468	Capitalization Grants for Drinking Water State Revolving Funds (Note 2) (Note 3d)	KIA	12,680,043		12,475,259
		NREPC	1,544,244		
66.470	Hardship Grants Program for Rural Communities	NREPC	19,444		19,444
66.471	State Grants to Reimburse Operators of Small Water Systems for Training and Certification Costs	NREPC	19,341		
66.474	Water Protection Grants to States	NREPC	8,388		
66.606	Surveys, Studies, Investigations and Special Purpose Grants (Note 13)	NREPC	529,954	168,990	
66.608	State Information Grants	NREPC	23,306		

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
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CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Environmental Protection Agency (Continued)</u>					
Direct Programs (Continued):					
66.700	Consolidated Pesticide Enforcement Cooperative Agreements	AGR	543,102		
66.701	Toxic Substances Compliance Monitoring Cooperative Agreements	NREPC	72,170		7,945
66.707	TSCA Title IV State Lead Grants Certification of Lead-Based Paint Professionals	CHS	245,806		
66.709	Capacity Building Grants and Cooperative Agreements for States and Tribes (Note 13)	NREPC		79,645	
66.801	Hazardous Waste Management State Program Support	NREPC	1,708,492		
66.802	Superfund State, Political Subdivision, and Indian Tribe Site-Specific Cooperative Agreements	NREPC	45,208		
66.804	State and Tribal Underground Storage Tanks Program	NREPC	186,675		
66.805	Leaking Underground Storage Tank Trust Fund Program	NREPC	1,151,242		
66.809	Superfund State and Indian Tribe Core Program-Cooperative Agreements	NREPC	109,380		
66.810	Chemical Emergency Preparedness and Prevention (CEPP) Technical Assistance Grants Program	NREPC	2,899		
66.817	State and Tribal Response Program Grants	NREPC	131,175		
Total U.S. Environmental Protection Agency			<u>\$ 36,756,979</u>	<u>\$ 248,635</u>	<u>\$ 21,939,563</u>
<u>U.S. Department of Energy</u>					
Direct Programs:					
81.039	Nation Energy Information Center	NREPC	\$ 7,523		\$
81.041	State Energy Program	NREPC	882,772		260,010
81.042	Weatherization Assistance for Low-Income Persons:	CFC	4,434,572		4,318,969
		CHS	7,632		
81.079	Regional Biomass Energy Programs	NREPC	15,000		
81.086	Conservation Research and Development	NREPC	343,070		
81.106	Transport of Transuranic Wastes to the Waste Isolation Pilot Plant: States and Tribal Concerns, Proposed Solutions (Note 14)	MIL			
81.117	Energy Efficiency and Renewable Energy Information Dissemination, Outreach, Training and Technical Analysis/Assistance	NREPC	85,914		52,625
81.119	State Energy Program Special Projects	NREPC	129,611		370,598
81.502	Paducah Gaseous Diffusion Plant Environmental Monitoring and Oversight	NREPC	1,084,887		278,674
		CHS	343,693		165,535
Total U.S. Department of Energy			<u>\$ 7,334,674</u>		<u>\$ 5,446,411</u>

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
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CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Department of Education</u>					
Direct Programs:					
84.002	Adult Education-State Grant Program (Note 2)	CPE	\$ 9,843,123		\$ 9,306,249
		MIL	125,363		
		CWD	59,578		46,344
84.010	Title I Grants to Local Educational Agencies (Note 2)	EDU	172,020,243		171,126,606
84.011	Migrant Education - State Grant Program	EDU	7,807,782		7,681,669
84.013	Title I Program for Neglected and Delinquent Children	JUV	602,956		489,238
		CORR	18,291		
		EDU	2,916		
Special Education Cluster:					
84.027	Special Education - Grants to States (Note 2)	EDU	114,867,690		112,538,361
84.173	Special Education - Preschool Grants (Note 2)	EDU	10,981,242		9,756,372
Student Financial Assistance Programs Cluster:					
84.032	Federal Family Education Loans (Note 2) (Note 3c)	KHEAA	50,907,494		
		KHESLC	36,604,117		
84.048	Vocational Education-Basic Grants to States (Note 2)	CWD	12,943,658		10,955,115
		EDU	10,440,083		10,198,715
84.069	Leveraging Educational Assistance Partnership	KHEAA	1,157,937		
84.116	Fund for the Improvement of Postsecondary Education	CPE	26,749		
84.126	Rehabilitation Services-Vocational Rehabilitation Grants to States (Note 2) (Note 9)	CWD	48,392,760		1,100,245
84.128	Rehabilitation Services-Service Projects	CWD	178,590		178,590
84.161	Rehabilitation Services-Client Assistance Program	CWD	168,402		
84.169	Independent Living-State Grants	CWD	355,620		12,046
84.177	Rehabilitation Services-Independent Living Services for Older Individuals Who are Blind	CWD	426,696		4,219
84.181	Special Education-Grants for Infants and Families with Disabilities	CCSHCN	5,187,730		
84.184	Safe and Drug-Free Schools and Communities-National Programs	EDU	721,923		721,923
84.185	Byrd Honors Scholarships	EDU	533,727		120,000
84.186	Safe and Drug-Free Schools and Communities-State Grants (Note 14)	EDU	6,246,832		5,956,726
		CHS	1,616,261		1,616,261
		GOV	24,832		
		KSP			
84.187	Supported Employment Services for Individuals with Severe Disabilities	CWD	483,174		
84.194	Bilingual Education Support Services	EDU	70,798		70,798
84.196	Education for Homeless Children and Youth	EDU	622,791		621,977
84.213	Even Start - State Educational Agencies	EDU	2,721,298		2,498,613
84.215	Fund for the Improvement of Education (Note 12)	EDU	531,886		516,031

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Department of Education (Continued)</u>					
Direct Programs (Continued):					
84.216	Private School-Capital Expenses	EDU	39,299		39,299
84.224	Assistive Technology	CWD	514,401		342,611
84.240	Program of Protection and Advocacy of Individual Rights	PUBAD	185,578		
84.243	Tech-Prep Education	CWD	1,990,781		1,936,284
84.265	Rehabilitation Training-State Vocational Rehabilitation Unit In-Service Training	CWD	158,936		
84.281	Eisenhower Professional Development State Grants	EDU	955,173		423,246
		CPE	203,506		203,286
84.287	Twenty-First Century Community Learning Centers	EDU	5,933,325		5,889,392
84.293	Foreign Language Assistance	EDU	29,587		
84.298	State Grants for Innovative Programs	EDU	6,024,213		5,656,592
84.318	Education Technology State Grants	EDU	8,127,071		7,678,501
84.323	Special Education-State Program Improvement Grants for Children with Disabilities	EDU	1,093,965		1,089,558
		CCSHCN	125,000		
84.326	Special Education - Technical Assistance and Dissemination to Improve Services and Results for Children with Disabilities	EDU	157,107		157,106
84.327	Special Education - Technology and Media Services for Individuals with Disabilities	EDU	69,822		69,822
84.330	Advanced Placement Program	EDU	474,287		85,661
84.331	Grants to States for Incarcerated Youth Offenders	CORR	205,834		
84.332	Comprehensive School Reform Demonstrator	EDU	3,836,312		3,645,960
84.334	Gaining Early Awareness and Readiness for Undergraduate Programs (Note 2)	CPE	2,356,448		1,705,930
84.336	Teacher Quality Enhancement Grants	EPSB	1,418,486		
84.340	Class Size Reduction	EDU	601,875		622,431
84.343	Assistive Technology - State Grants for Protection and Advocacy	PUBAD	67,801		
84.346	Vocational Education-Occupational and Employment Information State Grants	CWD	79,706		426
84.348	Title I Accountability Grants	EDU	2,019,826		2,019,826
84.352	School Renovation Grants	EDU	7,729,646		7,729,646
84.357	Reading First State Grants	EDU	2,813,053		2,002,070
84.358	Rural Education	EDU	3,287,282		3,276,308
84.365	English Language Acquisition Grants	EDU	1,345,309		1,310,816
84.366	Mathematics and Science Partnerships	EDU	337,215		337,130
84.367	Improving Teacher Quality State Grants (Note 2)	EDU	51,977,126		51,811,556
		CPE	628,033		620,205
84.369	Grants for State Assessments and Related Activities	EDU	2,593,220		32,566
<u>Passed Through From the Harlan Independent Board of Education:</u>					
84.215	Fund for the Improvement of Education Pass Through Grantor # - Various (Note 12)	KHS	280,298		

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Department of Education (Continued)</u>					
Passed Through From Bowling Green State University:					
84.304	Civic Education-Cooperative Education Exchange Program (Note 14) Pass Through Grantor # - Q304A030004 (Note 12)	AOC			
Passed Through From the Center for Civic Education:					
84.304	Civic Education-Cooperative Education Exchange Program Pass Through Grantor # - Q304B030001 (Note 12)	AOC	15,000		
84.929	We the People Pass Through Grantor # - Various (Note 12)	AOC	53,071		
Total U.S. Department of Education			\$ 604,420,134		\$ 444,202,326
<u>U.S. National Archives and Records Administration</u>					
Direct Programs:					
89.003	National Historical Publications and Records Grants	DLA	\$ 1,975		
Total U.S. National Archives and Records Administration			\$ 1,975		
<u>U.S. Department of Health and Human Services</u>					
Direct Programs:					
93.003	Public Health and Social Services Emergency Fund	CHS	\$ 2,890,626	\$	\$ 2,552,187
93.041	Special Programs for the Aging - Title VII, Chapter 3 - Programs for Prevention of Elder Abuse, Neglect, and Exploitation	CHS	70,771		70,771
93.042	Special Programs for the Aging - Title VII, Chapter 2 - Long Term Care Ombudsman Services for Older Individuals	CHS	187,648		105,137
93.043	Special Programs for the Aging - Title III, Part D - Disease Prevention and Health Promotion Services	CHS	338,908		338,908
<u>Aging Cluster:</u>					
93.044	Special Programs for the Aging - Title III, Part B - Grants for Supportive Services and Senior Centers	CHS	5,369,421		4,948,055
93.045	Special Programs for the Aging - Title III, Part C - Nutrition Services	CHS	7,835,081		7,520,006
93.046	Special Programs for the Aging - Title III, Part D - In-Home Services for Frail Older Individuals	CHS	602		602
93.048	Special Programs for the Aging - Title IV and Title II Discretionary Projects (Note 14)	CHS			
93.051	Alzheimer's Disease Demonstration Grants to State:	CHS	107,204		104,610

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Department of Health and Human Services (Continued)</u>					
<u>Direct Programs (Continued):</u>					
93.052	National Family Caregiver Support	CHS	1,953,942		1,865,215
93.053	Nutrition Services Incentive Program	CHS	1,822,646		1,822,646
93.104	Comprehensive Community Mental Health Services for Children with Serious Emotional Disturbances (SED)	CHS	947,881		936,305
93.110	Maternal and Child Health Federal Consolidated Program:	CCSHCN	172,712		
		CHS	116,135		69,870
		EDU	2,308		
93.116	Project Grants and Cooperative Agreements for Tuberculosis Control Programs (Note 13)	CHS	944,984	68,050	734,700
93.127	Emergency Medical Services for Childrer	EMSB	127,993		
93.130	Primary Care Services - Resource Coordination and Development	CHS	158,339		89,979
93.136	Injury Prevention and Control Research and State and Community Based Programs	CHS	1,097,862		1,084,169
93.138	Protection and Advocacy for Individuals with Mental Illness	PUBAD	425,276		
93.150	Projects for Assistance In Transition from Homelessness (PATH)	CHS	300,000		300,000
93.197	Childhood Lead Poisoning Prevention Projects - State and Local Childhood Lead Poisoning Prevention and Surveillance of Blood Lead Levels in Children	CHS	683,530		497,600
93.217	Family Planning - Services	CHS	6,259,625		5,812,423
93.230	Consolidated Knowledge Development and Application (KD&A) Program	CHS	90,527		90,412
93.234	Traumatic Brain Injury-State Demonstration Grant Program	CHS	169,500		169,400
		PUBAD	24,709		
93.235	Abstinence Education	CHS	1,100,585		1,040,616
93.238	Cooperative Agreements for State Treatment Outcomes and Performance Pilot Studies Enhancement	CHS	290,185		188,358
93.243	Substance Abuse and Mental Health Services-Projects of Regional and National Significance	CHS	131,881		131,499
93.251	Universal Newborn Hearing Screening	CCSHCN	165,158		
93.259	Rural Access to Emergency Devices Grant (Note 12)	EMSB	248,692		
93.268	Immunization Grants (Note 13)	CHS	2,607,372	14,471,378	1,475,316
93.283	Centers for Disease Control and Prevention-Investigations and Technical Assistance (Note 13)	CHS	14,530,567	1,100,802	10,061,885
		MIL	195,852		
		CCSHCN	191,508		
93.556	Promoting Safe and Stable Families	CFC	7,231,646		4,545,226
		CHS	873		

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
U.S. Department of Health and Human Services (Continued)					
Direct Programs (Continued):					
93.558	Temporary Assistance for Needy Families (Note 2) (Note 14)	CFC	118,478,048		11,770,701
		CWD	2,960,457		
		OAG	385,000		
		CHS	101,317		
		KHCORP			
93.563	Child Support Enforcement (Note 2)	CFC	39,783,680		34,280,228
		OAG	146,573		
		CHS	4,245		
93.568	Low-Income Home Energy Assistance (Note 2)	CFC	26,672,348		26,553,443
		CHS	15,771		
93.569	Community Services Block Grant	CFC	10,809,093		10,902,239
		CHS	16,435		
93.571	Community Services Block Grant Discretionary Awards- Community Food and Nutrition	CFC	59,978		59,978
Child Care Cluster:					
93.575	Child Care and Development Block Grant (Note 2)	CFC	68,103,955		4,881,424
93.596	Child Care Mandatory and Matching Funds of the Child Care and Development Fund (Note 2)	CFC	38,454,431		6,942,322
		CHS	1,927,537		
93.576	Refugee and Entrant Assistance - Discretionary Grants	EDU	183,845		183,844
93.585	Empowerment Zones Program	FAC	999,009		999,009
93.586	State Court Improvement Program	AOC	237,228		
93.590	Community-Based Family Resource and Support Grants	CFC	1,622,508		1,172,145
		AOC	18,565		
93.597	Grants to States for Access and Visitation Programs	CFC	144,026		144,026
93.599	Chafee Education and Training Vouchers Program (ETV)	CFC	216,382		
93.600	Head Start (Note 14)	EDU	112,192		
		GOV			
93.603	Adoption Incentive Payments	CFC	242,110		
93.618	Voting Access for Individuals with Disabilities-Grants for Protection and Advocacy Systems	PUBAD	8,989		
93.630	Developmental Disabilities Basic Support and Advocacy Grants	CHS	1,155,548		731,743
		PUBAD	547,771		
		CWD	98,296		12,483
93.631	Developmental Disabilities Projects of National Significance	CCSHCN	65,775		
93.643	Children's Justice Grants to States	CFC	146,322		132,418
		AOC	38,035		
93.645	Child Welfare Services-State Grants	CFC	4,438,136		
93.658	Foster Care-Title IV-E (Note 2)	CFC	49,903,456		23,674,704
		JUV	1,960,518		
		AOC	250,033		
		CHS	91,844		

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Department of Health and Human Services (Continued)</u>					
Direct Programs (Continued):					
93.659	Adoption Assistance	CFC	17,118,407		
93.667	Social Services Block Grant (Note 2)	CFC	18,332,053		916,389
		JUV	7,460,937		
		CHS	15,376		
93.669	Child Abuse and Neglect State Grants	CFC	323,142		71,070
93.671	Family Violence Prevention and Services/Grants for	CFC	984,025		981,979
	Battered Women's Shelters/Grants to State and Indian Tribes	CHS	123		
93.674	Chafee Foster Care Independent Living	CFC	1,547,338		1,097,275
		CHS	1,037		
93.767	State Children's Insurance Program (Note 2)	CHS	72,325,392		125,786
		CFC	314,699		
Medicaid Cluster:					
93.775	State Medicaid Fraud Control Units (Note 2)	OAG	1,138,958		
93.777	State Survey and Certification of Health Care Providers and Suppliers (Note 2)	CHS	5,593,098		
93.778	Medical Assistance Program (Note 2)	CHS	3,046,629,472		3,061,140
		CFC	18,045,422		
		OAG	106,500		
93.779	Centers for Medicare and Medicaid Services (CMS)	CHS	905,088		784,784
	Research, Demonstration and Evaluations	KHCORP	45,000		
93.917	HIV Care Formula Grants	CHS	6,938,917		6,888,398
93.931	Demnstration Grants to States for Community Scholarship (Note 14)	CHS			
93.938	Cooperative Agreements to Support Comprehensive School Health Programs to Prevent the Spread of HIV and Other Important Health Problems	EDU	481,012		381,322
		CHS	109,812		28,000
93.940	HIV Prevention Activities - Health Department Based (Note 13)	CHS	1,850,064	7,406	1,513,504
93.944	Human Immunodeficiency Virus (HIV)/Acquired Immunodeficiency Virus Syndrome (AIDS) Surveillance	CHS	136,265		34,476
93.945	Assistance Programs for Chronic Disease Prevention and Control	CHS	600,432		412,696
		EDU	29		
93.952	Improving EMS/Trauma Care in Rural Areas	EMSB	37,085		

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Department of Health and Human Services (Continued)</u>					
<u>Direct Programs (Continued):</u>					
93.958	Block Grants for Community Mental Health Services	CHS	5,716,331		5,705,193
		CWD	75,000		
		CORR	50,000		
		KHCORP	625		
93.959	Block Grants for Prevention and Treatment of Substance Abuse (Note 2)	CHS	21,420,937		21,415,754
		KSP	38,380		
		AOC	21,304		9,138
		KHCORP	625		
93.977	Preventive Health Services - Sexually Transmitted Diseases Control Grants (Note 13)	CHS	880,266	234,972	163,811
93.982	Mental Health Disaster Assistance and Emergency Mental Health	MIL	184,691		160,410
93.988	Cooperative Agreements for State-Based Diabetes Control Programs and Evaluation of Surveillance Systems	CHS	664,328		577,230
93.991	Preventive Health and Health Services Block Grant	CHS	1,794,377		1,639,656
93.994	Maternal and Child Health Services Block Grant to the States	CCSHCN	3,868,116		
		CHS	7,466,380		7,242,302
<u>Passed Through From the University of Kentucky:</u>					
93.259	Rural Access to Emergency Devices Grant Pass Through Grantor - 1H3DRH0000501 (Note 12)	EMSB	285,376		
Total U.S. Department of Health and Human Services			\$ 3,672,698,424	\$ 15,882,608	\$ 222,206,915
<u>U.S. Corporation for National and Community Service</u>					
<u>Direct Programs:</u>					
94.003	State Commissions	CFC	\$ 122,560		\$
94.004	Learn and Serve America-School and Community Based Programs (Note 14)	EDU	250,365		254,000
		CFC			
94.005	Learn and Serve America Higher Education	CPE	7,887		
94.006	AmeriCorps	CFC	1,440,733		1,394,360
		CHS	1,013		
94.007	Planning and Program Development Grants	CFC	41,455		18,688
		JUV	8,737		
94.009	Training and Technical Assistance	CFC	54,466		14,487
<u>Foster Grandparents/Senior Companion Cluster:</u>					
94.011	Foster Grandparent Program	CHS	597,829		124,796
94.NA(1)	Chemical Laboratory Improvement Act	CHS	158,941		
Total U.S. Corporation for National and Community Service			\$ 2,683,986		\$ 1,806,331

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>U.S. Social Security Administration</u>					
Direct Programs:					
Disability Insurance/SSI Cluster:					
96.001	Social Security-Disability Insurance (Note 2)	CFC	\$	39,680,721	
96.009	Social Security State Grants for Work Incentive Assistance to Disabled Beneficiaries	PUBAD		89,872	
Total U.S. Social Security Administration			\$	39,770,593	
<u>U. S. Department of Homeland Security</u>					
Direct Programs:					
97.004	State Domestic Preparedness Equipment Support Program (Note 14)	MIL	\$	11,166,939	\$
		KSP		474,910	
		NREPC		45,985	
		HBC		45,485	
		TC		7,678	
		COT		316	
		AGR			
97.012	Boating Safety Financial Assistance	F&W		660,142	
97.021	Hazardous Materials Assistance Program	MIL		3,966	
97.023	Community Assistance Program State Support Services Element (CAP-SSSE)	NREPC		128,866	27,000
97.029	Flood Mitigation Assistance (Note 14)	MIL			22,239
97.032	Crisis Counseling	MIL		161,118	47,671
97.035	Individual and Family Grants	MIL		371	
97.036	Public Assistance Grants (Note 2)	MIL		27,113,411	26,527,216
		TC		5,981,171	
97.039	Hazardous Mitigation Grant	MIL		3,399,482	2,670,304
97.040	Chemical Stockpile Emergency Preparedness Program	MIL		5,205,920	4,596,766
		CHS		374,726	115,805
97.041	National Dam Safety Program	NREPC		62,954	
97.042	Emergency Management Performance Grants	MIL		2,904,295	1,654,566
97.047	Pre-Disaster Mitigation	MIL		177,202	177,202
97.051	State and Local All Hazards Emergency Operations Planning	MIL		1,259,623	
97.052	Emergency Operations Centers	MIL		7,782	
97.053	Citizen Corps	MIL		300,706	205,886
97.054	Community Emergency Response Teams	MIL		150,665	143,750
Total U.S. Department of Homeland Security			\$	59,633,713	\$ 36,188,405

See accompanying Notes to the Schedule of Expenditures of Federal Awards

COMMONWEALTH OF KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FEDERAL ASSISTANCE PROGRAMS
FOR THE YEAR ENDED JUNE 30, 2004

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<u>Other Federal Assistance</u>					
Direct Programs:					
NA	Appalachia High Intensity Drug Trafficking Area	GOV	\$ 82,211		\$
NA	Joint Funding Administration (Note 8)	DLG	1,617,000		1,617,000
Total Other Federal Assistance			<u>\$ 1,699,211</u>		<u>\$ 1,617,000</u>
Total All State Organizations			<u>\$ 6,216,480,540</u>	<u>\$ 780,639,647</u>	<u>\$ 1,064,045,111</u>

See accompanying Notes to the Schedule of Expenditures of Federal Awards

COMMONWEALTH OF KENTUCKY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004

Note 1 - Purpose of the Schedule and Significant Accounting Policies

Basis of Presentation - OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, requires a Schedule of Expenditures of Federal Awards showing each federal financial assistance program as identified in the *Catalog of Federal Domestic Assistance*. The accompanying schedule includes all federal grant activity for the Commonwealth, except those programs administered by state universities, and is presented primarily on the basis of cash disbursements as modified by the application of Kentucky Revised Statute (KRS) 45.229. Consequently, certain expenditures are recorded in the accounts only when cash is disbursed. The Commonwealth elected to exclude state universities from the statewide single audit, except as part of the audit of the basic financial statements.

KRS 45.229 provides that the Finance and Administration Cabinet may, “for a period of thirty (30) days after the close of any fiscal year, draw warrants against the available balances of appropriations made for that fiscal year, for the payment of expenditures incurred during that year or in fulfillment of contracts properly made during the year, but for no other purpose.” However, there is an exception to the application of KRS 45.229 in that regular payroll expenses incurred during the last pay period of the fiscal year are charged to the next year.

The basic financial statements of the Commonwealth are presented on the modified accrual basis of accounting for the governmental fund financial statements and the accrual basis of accounting for the government-wide, proprietary fund, and fiduciary fund financial statements. Therefore, the schedule may not be directly traceable to the basic financial statements in all cases.

Noncash assistance programs are not reported in the basic financial statements of the Commonwealth for FY 04. The noncash expenditures presented on this schedule represent the noncash assistance expended using the method or basis of valuation described in Note 13.

Clusters of programs are indicated in the schedule by light gray shading.

Programs that do not have CFDA numbers are identified using the two-digit federal identifier prefix, and the letters “NA” to denote that no specific number is applicable. Each program is numbered in parentheses, following the NA for each federal grantor.

The state agencies’ schedule is presented on the cash, modified cash, or accrual basis of accounting.

**COMMONWEALTH OF KENTUCKY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Note 1 - Purpose of the Schedule and Significant Accounting Policies (Continued)

Inter-Agency Activity - Certain transactions relating to federal financial assistance may appear in the records of more than one (1) state agency. To avoid the overstatement of federal expenditures, the following policies were adopted for the presentation of the schedule:

- (a) Federal moneys may be received by a state agency and passed through to another state agency where the moneys are expended. Except for pass-throughs to state universities as discussed below, this inter-agency transfer activity is reported by the agency expending the moneys.

State agencies that pass federal funds to state universities report those amounts as expenditures.

- (b) Federal moneys received by a state agency and used to purchase goods or services from another state agency are reported in the schedule as an expenditure by the purchasing agency only.

Note 2 - Type A Programs

Type A programs for the Commonwealth mean any program for which total expenditures of federal awards exceeded \$20 million for FY 04. The Commonwealth had the following programs (cash and noncash) that met the Type A program definition for FY 04, some of which were administered by more than one (1) state agency. Certain component units and agencies audited by certified public accounting firms had lower dollar thresholds. The Commonwealth identified clusters among the Type A programs by gray shading. These Type A programs and clusters were:

CFDA #	Program Title	Expenditures
Food Stamp Cluster:		
10.551	Food Stamps	\$ 533,396,719
10.561	State Administrative Matching Grants for Food Stamp Program	27,821,607
Child Nutrition Cluster:		
10.553	School Breakfast Program	36,022,823
10.555	National School Lunch Program	110,671,808
10.556	Special Milk Program for Children	88,468
10.559	Summer Food Service Program for Children	6,154,494
10.557	Special Supplemental Nutrition Program for Women, Infants, and Children	88,002,978

COMMONWEALTH OF KENTUCKY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)

Note 2 - Type A Programs (Continued)

CFDA #	Program Title	Expenditures
10.558	Child and Adult Care Food Program	24,372,132
10.766	Community Facilities Loans and Grants	69,333,397
11.550	Public Telecommunications Facilities-Planning and Construction	807,505
14.117	Mortgage Insurance – Homes	124,331,475
Section 8 Project-Based Cluster:		
14.182	Lower Income Housing Assistance Program – Section 8 New Construction/Substantial Rehabilitation	84,425,207
14.856	Lower Income Housing Assistance Program – Section 8 Moderate Rehabilitation	87,934
14.228	Community Development Block Grants/State’s Program	31,038,022
14.235	Supportive Housing Program	3,511,592
14.871	Section 8 Housing Choice Vouchers	22,851,045
15.252	Abandoned Mine Land Reclamation (AMLR) Program	23,370,703
17.225	Unemployment Insurance	563,143,624
17.245	Trade Adjustment Assistance-Workers	21,569,133
Workforce Investment Act Cluster:		
17.258	WIA Adult Program	15,695,211
17.259	WIA Youth Activities	13,740,770
17.260	WIA Dislocated Workers	15,229,340
17.267	WIA Incentive Grants-Section 503 Grants to States	2,303,246
Highway Planning and Construction Cluster:		
20.205	Highway Planning and Construction	466,672,070
21.NA(2)	Job Growth Tax Relief Reconciliation Act	68,720,606
64.114	Veterans Housing-Guaranteed and Insured Loans	9,042,601
66.458	Capitalization Grants for Clean Water State Revolving Funds	8,525,898
66.468	Capitalization Grants for Drinking Water State Revolving Fund	14,224,287

COMMONWEALTH OF KENTUCKY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)

Note 2 - Type A Programs (Continued)

CFDA #	Program Title	Expenditures
84.002	Adult Education-State Grant Program	10,028,064
84.010	Title I Grants to Local Educational Agencies	172,020,243
Special Education Cluster:		
84.027	Special Education - Grants to States	114,867,690
84.173	Special Education – Preschool Grants	10,981,242
Student Financial Assistance Program Cluster:		
84.032	Federal Family Education Loans	87,511,611
84.048	Vocational Education-Basic Grants to States	23,383,741
84.126	Rehabilitation Services – Vocational Rehabilitation Grants to States	48,392,760
84.334	Gaining Early Awareness and Readiness for Undergraduate Programs	2,356,448
84.367	Improving Teacher Quality State Grants	52,605,159
93.558	Temporary Assistance for Needy Families	121,924,822
93.563	Child Support Enforcement	39,934,498
93.568	Low-Income Home Energy Assistance	26,688,119
Child Care Cluster:		
93.575	Child Care and Development Block Grant	68,103,955
93.596	Child Care Mandatory and Matching Funds of the Child Care and Development Fund	40,381,968
93.658	Foster Care-Title IV-E	52,205,851
93.667	Social Services Block Grant	25,808,366
93.767	State Children’s Insurance Program	72,640,091
Medicaid Cluster:		
93.775	State Medicaid Fraud Control Units	1,138,958
93.777	State Survey and Certification of Health Care Providers and Suppliers	5,593,098
93.778	Medical Assistance Program	3,064,781,394
93.959	Block Grants for Prevention and Treatment of Substance Abuse	21,481,246

COMMONWEALTH OF KENTUCKY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)

Note 2 - Type A Programs (Continued)

CFDA #	Program Title	Expenditures
Disability Insurance/SSI Cluster:		
96.001	Social Security – Disability Insurance	39,680,721
97.036	Public Assistance Grants	33,094,582
Total Type A Programs		\$6,520,759,322

Note 3 - Federally Assisted Loan Programs

The Commonwealth has several loan programs made possible with initial advances in prior years from the federal government. In addition, the federal government guarantees some loan programs.

a) The Kentucky Rural Rehabilitation Student Loan Program was initially awarded \$672,629 in 1970 by the U. S. Farmers Home Administration. Since 1970, the program has operated on interest from student loans outstanding and on income from investments administered by the Office of Financial Management. The Department of Agriculture is no longer in the business of making student loans and reassigned all loans in payment compliance to the Kentucky Higher Education Assistance Authority (KHEAA). The Department of Agriculture retained only those loans that had a delinquent payment history. This program is currently in phase-out status, with authorization from the U. S. Department of Agriculture (USDA) to eliminate the principal through issuance of specific grants and scholarships. Most outstanding loans have been classified as contingent uncollectible liabilities. When loan payments are received, they are directly deposited into the principal account. The total amount of money in the investment account as of June 30, 2004 was \$654,107. Student loans and investment earned interest of \$26,706. Outstanding student loans totaled \$64,466. The total grants and scholarships authorized by the USDA in FY 04 totaled \$111,383.

b) Total moneys for the Gas System Restoration Project, administered by the Department for Local Government (CFDA #11.307), consist of \$3,150,000 from the U.S. Economic Development Administration; \$500,000 from the U.S. Appalachian Regional Commission; and, \$650,000 in state matching money, for a total commitment to the revolving loan program of \$4,300,000. All monies had been received and paid out by June 30, 2004. In addition, principal and interest repaid is available for lending.

c) The Kentucky Higher Education Student Loan Corporation (KHESLC) issues revenue bonds in order to purchase student loans authorized under the Federal Family Education Loans program (CFDA #84.032). The KHEAA guarantees substantially all loans made

COMMONWEALTH OF KENTUCKY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)

Note 3 - Federally Assisted Loan Programs (Continued)

and purchased by the KHESLC. The U.S. Department of Education provides for reinsurance of loans guaranteed by the KHEAA. Outstanding loans guaranteed under this program totaled \$2,908,356,000 as of June 30, 2004.

d) The Kentucky Infrastructure Authority administers wastewater revolving loan programs (CFDA #66.458 and 66.468) funded by the U.S. Environmental Protection Agency's Capitalization Grants for State Revolving Funds. During the year ended June 30, 2004, the Authority issued loans totaling \$20,467,546, with outstanding loans of \$283,995,320 at year-end.

e) The Department of Housing and Urban Development's Mortgage Insurance-Homes (CFDA #14.117), Department of Agriculture's Community Facilities Loans and Grants (CFDA #10.766), and Department of Veterans Affairs' Veterans Housing-Guaranteed and Insured Loans (CFDA #64.114) represent the loans originated in FY 04 by the Kentucky Housing Corporation. The cumulative outstanding balance of the Mortgage Insurance Program, Community Facilities Loans and Grants Program, and Veterans Housing and Guaranteed Loans Program loans originated by the Kentucky Housing Corporation is \$704,859,143, \$277,960,985, and \$65,766,125, respectively at June 30, 2004.

Note 4 - Activity Occurring in Programs with Inventoriable Items

The Department of Agriculture operates a warehouse in Louisville, Kentucky for the Commodity Supplemental Food Program (CFDA #10.565). The dollar value of the inventory, based on the USDA Commodity File dated July 2003 is as follows:

	Commodity Supplemental Food Program CFDA #10.565
Beginning Inventory, July 1, 2003	\$ 426,093
Received	2,792,405
Issued to Recipients	(3,096,139)
Ending Inventory, June 30, 2004	\$ 122,359

**COMMONWEALTH OF KENTUCKY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Note 5 - Unemployment Insurance (CFDA #17.225)

The Commonwealth paid out \$530,010,492 in benefits in FY 04. The amounts shown on the accompanying schedule reflect both the amount expended for benefits from the Trust Fund and an additional \$33,133,132 of federal funds expended for administration of the program, resulting in a combined total of \$563,143,624 in federal expenditures.

Note 6 - Highway Planning and Construction (CFDA #20.205)

The information reported for this program represents the activity of all open projects during FY 04. These projects were funded from several apportionments. Apportionments refer to a federal, statutorily prescribed division or assignment of funds. The expenditures reflected on the schedule include expenditures for advance construction projects, which are not yet under agreements with the Federal Highway Administration.

Program Income - The Highway Planning and Construction Program earned program income of \$456,068 in FY 04. This income was earned in the right-of-way phase through the sale and rental of real property. Income earned in this manner was classified as a negative expenditure, resulting in a reduction to federal expenditures for the current year.

Refunds - Expenditures for the Highway Planning and Construction Program were shown net of any refunds, resulting from a reimbursement of prior or current year expenditures. Refunds totaled \$1,631,354 for FY 04.

Note 7 - Outdoor Recreation - Acquisition, Development and Planning (CFDA # 15.916) and Recreational Trails Program (CFDA # 20.219)

Administrative costs are shown as expended when received from the federal government. These costs are recovered through a negotiated, fixed-indirect cost rate. Any over or under recovery will be recouped in the future.

Note 8 - Joint Funding Administration

The Joint Funding Administration Program (listed in the schedule under Other Federal Assistance) consists of grants from the following federal agencies:

- U.S. Department of Commerce
- U.S. Department of Housing and Urban Development
- U.S. Appalachian Regional Commission
- Delta Regional Authority

COMMONWEALTH OF KENTUCKY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)

Note 9 - Research and Development Expenditures

OMB Circular A-133 Section 105 states, "Research and development (R&D) means all research activities, both basic and applied, and all development activities that are performed by a non-federal entity."

The expenditures presented in the SEFA include R&D expenditures. The R&D portion of the expenditures for each program is listed below.

CFDA #	Program Title	State Organization	Expenditures
10.028	Wildlife Services	F&W	\$ 40,649
15.605	Sport Fish Restoration	F&W	1,339,845
15.615	Cooperative Endangered Species Conservation Fund	F&W	82,807
15.625	Wildlife Conservation and Restoration	F&W	11,666
15.634	State Wildlife Grants	F&W	35,354
16.579	Byrne Formula Grant Program	AOC	62,470
16.585	Drug Court Discretionary Grant Program	AOC	88,534
39.011	Election Reform Payments	BOE	9,523
84.126	Rehabilitation Services-Vocational Rehabilitation Grants to States	CWD	89,714
Total R&D Expenditures			\$1,760,562

Note 10 - Community Development Block Grants/State's Program (CFDA #14.228)

The Commonwealth matches the federal portion of administration dollar for dollar. Cash expenditures include the federal portion of administration.

Note 11 - Wildlife Restoration (CFDA #15.611)

The Department of Fish and Wildlife Resources leases properties from the U.S. Army Corp of Engineers for Condition Three and Condition Five Projects. These projects stipulate that the properties leased be managed for wildlife purposes and may produce income. The leases for wildlife management rights on these properties are non-monetary. The Department of Fish and Wildlife Resources currently leases the following properties:

- Barren River
- Green River
- Dewey Lake
- Fishtrap Lake

**COMMONWEALTH OF KENTUCKY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Note 11 - Wildlife Restoration (CFDA #15.611) (Continued)

Any expenditure in excess of revenue from each property listed above will be eligible for reimbursement under the Wildlife Restoration grant (CFDA # 15.611) from the U.S. Department of the Interior. The properties listed above are not reimbursed with federal funds, if the grant has already been expended to manage other wildlife properties.

Note 12 - Pass Through Programs

OMB Circular A-133 Section 105 defines a recipient as “a non-Federal entity that expends Federal awards received directly from a Federal awarding agency to carry out a Federal program” and a pass-through entity as “a non-Federal entity that provides a Federal award to a subrecipient to carry out a Federal program.”

Federal program funds can be received directly from the federal government or passed through from another entity. Below is a list of all federal programs that are either (1) passed through, or (2) both direct and passed through.

Received From	Direct/Pass Through (Grantor #)	State Agency	Amount
<u>Public Safety Partnership and Community Policing Grants (CFDA #16.710)</u>			
U.S. Department of Justice	Direct	KSP	\$ 533,209
Eastern Kentucky University	Direct	JUST	
	Pass Through (97-CK-WK-1)	DCJT	
Total Public Safety Partnership and Community Policing Grants			<u>\$ 533,209</u>
<u>Fund for the Improvement of Education (CFDA #84.215)</u>			
U.S. Department of Education	Direct	EDU	\$ 531,886
Harlan Independent Board of Education	Pass Through (Various)	KHS	280,298
Total Fund for the Improvement of Education			<u>\$ 812,184</u>

COMMONWEALTH OF KENTUCKY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)

Note 12 – Pass Through Programs (Continued)

Received From	Direct/Pass Through (Grantor #)	State Agency	Amount
<u>Civic Education – Cooperative Education Exchange Program (CFDA #84.304)</u>			
Bowling Green State University	Pass Through (Q304A030004)	AOC	\$
Center for Civic Education	Pass Through (Q304B030001)	AOC	15,000
Total Civic Education – Cooperative Education Exchange Program			<u>\$ 15,000</u>

We the People (CFDA #84.929)

Center for Civic Education	Pass Through (Various)	AOC	\$ 53,071
Total We The People			<u>\$ 53,071</u>

Rural Access To Emergency Devices Grant (CFDA #93.259)

U.S. Department of Health and Human Services	Direct	EMSB	\$ 248,692
Center for Civic Education	Pass Through (1H3DRH0000501)	EMSB	285,376
Total Rural Access To Emergency Devices Grant			<u>\$ 534,068</u>

Note 13 – Noncash Expenditure Programs

The Commonwealth's noncash programs and a description of the method/basis of valuation follow.

CFDA #	Program Title	Amount	Method/Basis of Valuation
10.550	Food Donation	\$ 18,078,056	Commodities issued per ECOS Report dated September 15, 2004.
10.550	Food Donation	179,522	Active Commodity file report dated November, 2003.
10.551	Food Stamps	533,396,719	Electronic Benefit Transfer Issuance

**COMMONWEALTH OF KENTUCKY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Note 13 – Noncash Expenditure Programs (Continued)

10.565	Commodity Supplemental Food Program	3,096,139	Quantity issued to recipients valued at USDA's April 2004 Commodity File.
10.569	Emergency Food Assistance Program (Food Commodities)	5,740,332	Quantity issued to recipients valued at USDA's April 2004 Commodity File.
10.664	Cooperative Forestry Assistance	572,027	Determined by Federal government.
10.766	Community Facilities Loans and Grants	69,333,397	Book value of loans.
10.914	Wildlife Habitat Incentive Program	5,250	25% of agreement total (\$21,000).
14.117	Mortgage Insurance-Homes	124,331,475	Book value of loans.
15.250	Regulation of Surface Coal Mining and Surface Effects of Underground Coal Mining	35,802	Controlled property inventory.
15.808	U.S. Geological Survey - Research and Data Collection	58,500	Half of investigation cost at Maxey Flats.
39.003	Donation of Federal Surplus Personal Property	627,599	23.3% of federal acquisition cost (\$2,693,561).
43.NA(1)	Kentucky Landscape Snapshot	10,985	Equipment received in lieu of personnel dollars.
64.114	Veterans Housing - Guaranteed and Insured Loans	9,042,601	Book value of loans.
66.606	Surveys, Studies, Investigations and Special Purpose Grants	168,990	EPA and National Parks air monitoring contract and actual cost of filters purchased by EPA for NREPC.

**COMMONWEALTH OF KENTUCKY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Note 13 – Noncash Expenditure Programs (Continued)

66.709	Capacity Building Grants and Cooperative Agreements for States and Tribes	79,645	Contract Proposal/Billing.
93.268	Immunization Grants	14,471,378	Per authorized award for personnel, vaccine costs, and travel.
93.283	Centers for Disease Control and Prevention-Investigations and Technical Assistance	1,100,802	Per authorized award.
93.940	HIV Prevention Activities - Health Department Based	7,406	Per authorized award.
93.977	Preventive Health Services - Sexually Transmitted Diseases Control Grants	234,972	Per authorized award.
Total Noncash Expenditures		<u>\$ 780,571,597</u>	

Note 14 - Zero Expenditure Programs

These programs had no expenditures related to the respective state organization during FY 04. The zero expenditure programs included programs with no activity during the year, such as old programs not officially closed out or new programs issued late in the fiscal year. They also included programs with activity other than expenditures. For CFDA numbers with multiple state organizations listed, the schedule is presented in descending expenditure amount order.

Note 15 – Adult Education – State Grant Program (CFDA #84.002)

During FY 04, as a result of and Executive Order issued by the Governor of the Commonwealth of Kentucky, the Department of Adult Education and Literacy (DAEL) within the Cabinet for Workforce Development was abolished. All functions and activities associated with adult education and literacy were assigned to the Council on Postsecondary Education. All receipts and expenditures for grants prior to FY 04 for DAEL, were accounted for by the Cabinet for Workforce Development.

REPORTS ON COMPLIANCE AND ON INTERNAL CONTROL



CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

Report on Internal Control Over Financial Reporting
and on Compliance and Other Matters Based on an Audit of Financial Statements
Performed in Accordance With
Government Auditing Standards

Honorable Ernie Fletcher, Governor
Cabinet Secretaries and Agency Heads
Members of the Commonwealth of Kentucky Legislature

We have audited the financial statements of the governmental activities, business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Commonwealth of Kentucky as of and for the year ended June 30, 2004, which collectively comprise the Commonwealth's basic financial statements and have issued our report thereon dated December 23, 2004. Several agencies were tested for compliance and internal control requirements in accordance with *Government Auditing Standards* by other auditors, whose reports thereon have been furnished to us.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Commonwealth's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Commonwealth's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items 04-CFC1-1, 04-CFC2-2, 04-CWD1-3, 04-CWD2-4, 04-CWD3-5, 04-FAC1-6, 04-FAC2-7, 04-FAC3-8, 04-FAC4-9, 04-FAC5-10, 04-PARKS1-11, 04-REV1-12, 04-TC1-13, 04-TC2-14, 04-TC3-15, 04-TC4-16, and 04-TC5-17.



Report on Internal Control Over Financial Reporting
and on Compliance and Other Matters Based on an Audit of
Financial Statements Performed in Accordance With
Government Auditing Standards
(Continued)

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that none of the reportable conditions described above is a material weakness. We also noted other matters involving internal control over financial reporting, which we have reported to management.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Commonwealth's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance and other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as item 04-CWD3-5, 04-FAC3-8, and 04-PARKS1-11. We also noted certain additional matters that we reported to management in a separate letter.

Report on Internal Control Over Financial Reporting
and on Compliance and Other Matters Based on an Audit of
Financial Statements Performed in Accordance With
Government Auditing Standards
(Continued)

This report is intended solely for the information and use of the management, members of the legislature, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,

A handwritten signature in black ink, appearing to read "Crit Luallen", with a long horizontal flourish extending to the right.

Crit Luallen
Auditor of Public Accounts

December 23, 2004



CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

Report on Compliance With Requirements Applicable to Each
Major Program and on Internal Control Over Compliance in
Accordance With OMB Circular A-133 and on the
Schedule of Expenditures of Federal Awards

Honorable Ernie Fletcher, Governor
Cabinet Secretaries and Agency Heads
Members of the Commonwealth of Kentucky Legislature

Compliance

We have audited the compliance of the Commonwealth of Kentucky with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2004. Several agencies were audited for compliance requirements in accordance with OMB Circular A-133 by other auditors, whose reports thereon have been furnished to us, and our opinion presented herein, insofar as it relates to these agencies listed in Appendix 1 to this report, is based on the reports of the other auditors.

The Commonwealth's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Commonwealth's management. Our responsibility is to express an opinion on the Commonwealth's compliance based on our audit.

The Commonwealth's basic financial statements included the operations of the state universities, which expended \$659,908,246 in federal awards that are not included in the schedule of expenditures of federal awards for the year ended June 30, 2004. Our audit, described below, did not include the operations of the state universities because they engaged other auditors to perform an audit in accordance with OMB Circular A-133.



Report on Compliance With Requirements Applicable to Each
Major Program and on Internal Control Over Compliance in
Accordance With OMB Circular A-133 and on the
Schedule of Expenditures of Federal Awards
(Continued)

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Commonwealth's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Commonwealth's compliance with those requirements.

As described in items 04-DMA4-48 and 04-DMA5-49 in the accompanying schedule of findings and questioned costs, the Department of Military Affairs did not comply with requirements regarding subrecipient monitoring that are applicable to its State Domestic Preparedness Equipment Support Program (CFDA 97.004) and its Public Assistance Grants (CFDA 97.036). Compliance with such requirements is necessary, in our opinion, for the Department of Military Affairs to comply with the requirements applicable to those programs.

In our opinion, based on our audit and the reports of other auditors, except for the noncompliance described in the preceding paragraph, the Commonwealth complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2004. However, the results of our auditing procedures disclosed other instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 04-CFC7-19, 04-CFC8-20, 04-CFC9-21, 03-CFC10-22, 04-CWD12-28, 04-DFWR2-30, 04-DFWR3-31, 04-DMA1-32, 04-DMA2-33, 04-DMA3-34, 04-DVA2-36, 04-JUST1-37, 04-JUST2-38, 04-JUST3-39, 04-JUST4-40, 04-JUST5-41, 04-NREPC1-42, 04-TC10-44, 04-TC11-45, and 04-TC13-47. We also noted certain immaterial instances of noncompliance, which we have reported to management in a separate letter.

Internal Control Over Compliance

The management of the Commonwealth is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Commonwealth's internal control over compliance with

Report on Compliance With Requirements Applicable to Each
Major Program and on Internal Control Over Compliance in
Accordance With OMB Circular A-133 and on the
Schedule of Expenditures of Federal Awards
(Continued)

requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the Commonwealth's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items 04-CFC6-18, 04-CFC7-19, 04-CFC10-22, 04-CHS1-23, 04-CHS2-24, 04-CWD9-25, 04-CWD10-26, 04-CWD11-27, 04-CWD12-28, 04-DFWR1-29, 04-DFWR3-31, 04-DMA1-32, 04-DMA2-33, 04-DMA3-34, 04-DMA4-48, 04-DMA5-49, 04-DVA1-35, 04-JUST1-37, 04-JUST2-38, 04-JUST3-39, 04-JUST4-40, 04-JUST5-41, 04-TC9-43, 04-TC12-46, and 04-TC13-47.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider items 04-DMA4-48 and 04-DMA5-49 to be material weaknesses. We also noted other matters involving internal control over compliance, which we have communicated to management in a separated letter.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Commonwealth as of and for the year ended June 30, 2004, and have issued our report thereon dated December 23, 2004. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the Commonwealth's basic financial statements. The

Report on Compliance With Requirements Applicable to Each
Major Program and on Internal Control Over Compliance in
Accordance With OMB Circular A-133 and on the
Schedule of Expenditures of Federal Awards
(Continued)

accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements taken as a whole.

Several schedules of expenditures of federal awards were audited by other auditors, whose reports thereon have been furnished to us, and our opinion presented herein, insofar as it relates to these agencies listed in Appendix 1 to this report, is based on the reports of the other auditors.

The basic financial statements of the Commonwealth are prepared on an accrual/modified accrual basis of accounting. However, the schedule of expenditures of federal awards of the Commonwealth is prepared on the basis of cash disbursements as modified by the application of KRS 45.229. Consequently, certain expenditures are recorded in the accounts only when cash is disbursed. Accordingly, the schedule of expenditures of federal awards is not intended to present the expenditures of federal awards in conformity with accounting principles generally accepted in the United States of America.

In our opinion, based on our audit and the reports of other auditors, except for the effect of the application of a different basis of accounting, as explained above, the schedule of expenditures of federal awards is fairly stated, in all material respects, in relation to the Commonwealth's basic financial statements taken as a whole.

This report is intended solely for the information and use of the management, members of the legislature, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,

A handwritten signature in black ink, appearing to read "Crit Luallen", written in a cursive style.

Crit Luallen
Auditor of Public Accounts

Schedule of Expenditures of Federal Awards
December 23, 2004

February 28, 2005

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004**

SECTION 1 – SUMMARY OF AUDITOR’S RESULTS

Financial Statements

Financial Statements: We issued an unqualified opinion on the basic financial statements of the Commonwealth for the year ended June 30, 2004.

Compliance: In relation to the audit of the basic financial statements of the Commonwealth, and the Schedule of Expenditures of Federal Awards, the results of our tests disclosed three (3) instances of noncompliance that are required to be reported under *Government Auditing Standards*. We believe the instances of noncompliance are not material.

<u>STATE ORGANIZATION</u>	<u>REPORTABLE</u>	<u>MATERIAL</u>
Cabinet for Workforce Development (04-CWD3-5)	1	
Department of Parks (04-PARKS1-11)	1	
Finance and Administration Cabinet (04-FAC3-8)	1	

Internal Control Over Financial Reporting: Our consideration of the Commonwealth’s internal control over financial reporting disclosed 17 reportable conditions. We believe none of the reportable conditions are material weaknesses.

<u>STATE ORGANIZATION</u>	<u>REPORTABLE</u>	<u>MATERIAL</u>
Cabinet for Families and Children (04-CFC1-1, 04-CFC2-2)	2	
Cabinet for Workforce Development (04-CWD1-3, 04-CWD2-4, 04-CWD3-5)	3	
Department of Parks (04-PARKS1-11)	1	
Department of Revenue (04-REV1-12)	1	
Finance and Administration Cabinet (04-FAC1-6, 04-FAC2-7, 04-FAC3-8, 04-FAC4-9, 04-FAC5-10)	5	
Transportation Cabinet (04-TC1-13, 04-TC2-14, 04-TC3-15, 04-TC4-16, 04-TC5-17)	5	

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 1 – SUMMARY OF AUDITOR’S RESULTS (CONTINUED)

Federal Awards and Schedule of Expenditures of Federal Awards

Compliance: We issued a qualified opinion on the Commonwealth’s compliance with the requirements applicable to each of its major federal programs. The results of our auditing procedures disclosed 22 instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133. We believe two (2) of the instances of noncompliance are material.

<u>STATE ORGANIZATION</u>	<u>REPORTABLE</u>	<u>MATERIAL</u>
Cabinet for Families and Children (04-CFC7-19, 04-CFC8-20, 04-CFC9-21, 04-CFC10-22)	4	
Cabinet for Workforce Development (04-CWD12-28)	1	
Department of Fish & Wildlife Resources (04-DFWR2-30, 04-DFWR3-31)	2	
Department of Military Affairs (04-DMA1-32, 04-DMA2-33, 04-DMA3-34 04-DMA4-48, 04-DMA5-49)	3	2
Department of Veterans Affairs (04-DVA2-36)	1	
Justice Cabinet-Office of the Secretary (04-JUST1-37, 04-JUST2-38, 04-JUST3-39, 04-JUST4-40, 04-JUST5-41)	5	
Natural Resources and Environmental Protection Cabinet (04-NREPC1-42)	1	
Transportation Cabinet (04-TC10-44, 04-TC11-45, 04-TC13-47)	3	

Internal Control Over Compliance: Our consideration of the Commonwealth’s internal control over compliance disclosed 25 reportable conditions. We believe that two (2) of the reportable conditions are material weaknesses.

<u>STATE ORGANIZATION</u>	<u>REPORTABLE</u>	<u>MATERIAL</u>
Cabinet for Families and Children (04-CFC6-18, 04-CFC7-19, 04-CFC10-22)	3	
Cabinet for Health Services (04-CHS1-23, 04-CHS2-24)	2	

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 1 – SUMMARY OF AUDITOR’S RESULTS (CONTINUED)

Federal Awards and Schedule of Expenditures of Federal Awards (Continued)

<u>STATE ORGANIZATION</u>	<u>REPORTABLE</u>	<u>MATERIAL</u>
Cabinet for Workforce Development (04-CWD9-25, 04-CWD10-26, 04-CWD11-27, 04-CWD12-28)	4	
Department of Fish & Wildlife Resources (04-DFWR1-29, 04-DFWR3-31)	2	
Department of Military Affairs (04-DMA1-32, 04-DMA2-33, 04-DMA3-34 04-DMA4-48, 04-DMA5-49)	3	2
Department of Veterans Affairs (04-DVA1-35)	1	
Justice Cabinet-Office of the Secretary (04-JUST1-37, 04-JUST2-38, 04-JUST3-39, 04-JUST4-40, 04-JUST5-41)	5	
Transportation Cabinet (04-TC9-43, 04-TC12-46, 04-TC13-47)	3	

Schedule of Expenditures of Federal Awards: We issued a qualified opinion on the Commonwealth’s Schedule of Expenditures of Federal Awards because of the effect of the application of a different basis of accounting that is not in conformity with accounting principles generally accepted in the United States of America as described in Note 1 of the schedule. The opinion was issued in relation to the basic financial statements of the Commonwealth taken as a whole.

Identification of Major Programs

The following is a list of major Type A programs:

<u>CFDA #</u>	<u>Program Title</u>
Food Stamp Cluster:	
10.551	Food Stamps
10.561	State Administrative Matching Grants for Food Stamp Program
10.557	Special Supplemental Nutrition Program for Women, Infants, and Children
10.766	Community Facilities Loans and Grants
11.550	Public Telecommunications Facilities – Planning and Construction

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 1 – SUMMARY OF AUDITOR’S RESULTS (CONTINUED)

Identification of Major Programs (Continued)

- 14.117** Mortgage Insurance-Homes
- 14.182** Lower Income Housing Assistance Program-Section 8 New Construction/Substantial Rehabilitation
- 14.235** Supportive Housing Program
- 15.252** Abandoned Mine Land Reclamation (AMLR) Program
- 17.245** Trade Adjustment Assistance – Workers

Workforce Investment Act Cluster:

- 17.258** WIA Adult Program
- 17.259** WIA Youth Activities
- 17.260** WIA Dislocated Workers

Highway Planning and Construction Cluster:

- 20.205** Highway Planning and Construction

- 21.NA(2)** Jobs and Growth Tax Relief Reconciliation Act
- 64.114** Veterans Housing-Guaranteed and Insured Loans
- 66.458** Capitalization Grants for Clean Water State Revolving Funds
- 66.468** Capitalization Grants for Drinking Water State Revolving Funds
- 84.002** Adult Education – State Grant Program
- 84.334** Gaining Early Awareness and Readiness for Undergraduate Programs
- 84.367** Improving Teacher Quality State Grants

Student Financial Assistance Programs Cluster:

- 84.032** Federal Family Education Loans

- 93.558** Temporary Assistance for Needy Families
- 93.563** Child Support Enforcement

Child Care Cluster:

- 93.575** Child Care and Development Block Grant
- 93.596** Child Care Mandatory and Matching Funds of the Child Care and Development Fund

- 93.658** Foster Care – Title IV – E
- 93.767** State Children’s Insurance Program

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 1 – SUMMARY OF AUDITOR’S RESULTS (CONTINUED)

Identification of Major Programs (Continued)

Medicaid Cluster:

93.775	State Medicaid Fraud Control Units
93.777	State Survey and Certification of Health Care Providers and Suppliers
93.778	Medical Assistance Program

97.036 Public Assistance Grants

The following is a list of major Type B programs:

CFDA #	Program Title
12.401	National Guard Military Operations and Maintenance (O & M) Projects
15.250	Regulation of Surface Coal Mining and Surface Effects of Underground Coal Mining
Fish and Wildlife Cluster:	
15.605	Sport Fish Restoration
15.611	Wildlife Restoration
16.575	Crime Victim Assistance
16.579	Byrne Formula Grant Program
16.588	Violence Against Women Formula Grants
Employment Services Cluster:	
17.207	Employment Service
17.801	Disabled Veterans’ Outreach Program (DVOP)
17.804	Local Veterans’ Employment Representative Program
17.503	Occupational Safety and Health – State Program
Federal Transit Cluster:	
20.500	Federal Transit – Capital Investment Grants
20.509	Formula Grants for Other Than Urbanized Areas
64.203	State Cemetery Grants
84.318	Education Technology State Grants
97.004	State Domestic Preparedness Equipment Support Program

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 1 – SUMMARY OF AUDITOR’S RESULTS (CONTINUED)

Dollar Threshold Used to Distinguish Between Type A and Type B Programs

The maximum dollar threshold used to distinguish between Type A and Type B Programs was \$20 million. Certain component units and agencies audited by Certified Public Accountant (CPA) firms had lower dollar thresholds.

Auditee Risk

The Commonwealth did not qualify as a low-risk auditee.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

***Reportable Conditions Relating to Internal Controls and/or Reportable
Instances of Noncompliance:***

**FINDING 04-CFC1-1: The Cabinet For Families And Children Password Policy
Should Be Consistently Applied To All Local Area Network Servers**

State Organization: Cabinet for Families and Children

As was noted in the previous audit, CFC did not ensure password policies established on machines adhered to the agency-established password policies. During security vulnerability testing for machines controlled by CFC during FY 04, the auditor received account related information from seven (7) machines within two (2) CFC domains. This information was compared to the agency-established password policy criteria. See the table below for a summary of our findings.

Security Measure	Standard	Number of machines not in compliance with policy	Percentage of 7 machines not in compliance with policy
Maximum Age	31 days	5 – 42 days 1 – 30 days	85.7%
Minimum Age	1 day	5 – None	71.4%
Minimum Length	8 characters	5 – None	71.4%
Lockout Threshold	3 attempts	5 – None 1 – 4 attempts 1 – 5 attempts	100%
Lockout Duration	60 minutes	4 – 30 minutes 1 – 71582788 min 1 – None	85.7%
Lockout Reset	30 minutes	1 – 90 minutes 1 – 60 minutes 1 – None	42.9%

One (1) of these machines was noted with the same password policy issues in the prior year report comment. In addition, one (1) of these machines does not force users to logoff and the password history length is not tracked. This particular machine was noted as not complying with the established password policy in the prior audit report.

If machines within a network are not sufficiently secured, the network could be compromised.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

**FINDING 04-CFC1-1: The Cabinet For Families And Children Password Policy
Should Be Consistently Applied To All Local Area Network Servers (Continued)**

Passwords are an important aspect of computer security. They are the front line of protection for system access. To help ensure the security of a network, it is necessary for a strong password policy to be developed and implemented on all servers within the network in a consistent manner.

Recommendation

We recommend CFC review all machines within their agency-owned domains to ensure that the password policies established complies with the policy established by the agency.

Management's Response and Corrective Action Plan

There are two types of password policy in our environment, one being the domain password policy and the other being the local password policy, which resides on each workstation and server on our network. The domain policy is the most critical of the two, and all Cabinet for Health and Family Services (CHFS) user accounts use the domain accounts to access resources on our network. CHFS domain policies are in compliance with COT standards, with the exception of Local Health Departments (LHD). We are currently in the process of bringing the LHDs into compliance using an incremental approach. The local policies will be brought into compliance in the AD domain through the use of Group Policy Objects (GPO). Our current environment would require a manual reconfiguration of each machine and would be extremely resource intensive. The use of GPOs in the AD Domain would allow us to correct this on all machines by simply applying the policy at the domain level. Any servers listed in the detailed report that are out of compliance will be immediately addressed.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING: 04-CFC2-2: The Cabinet For Families And Children Should Ensure All Inactive Accounts Are Eliminated And That All Account Names Are Ambiguous

State Organization: Cabinet for Families and Children

During the security vulnerability testing for FY 04 on machines controlled by CFC, NetBIOS account information was received from eight (8) machines, including a Primary Domain Controller (PDC) and Backup Domain Controller (BDC) machine, and six (6) Structured Query Language (SQL) and New Technology (NT) machines.

To determine possible unnecessary accounts, the auditor used the criteria that the account password was over the 31-day maximum age and had been used to log onto the system at some point. Fourteen administrator accounts, nine (9) of which are on the PDC, and 87 user accounts, all on the PDC, met this criterion. In addition, there were nine (9) accounts on the PDC that were listed as disabled. Further, the PDC and BDC machines examined had several accounts that had never logged into the system.

Two (2) SQL/NTS machines had the default administrator account that had not been renamed. If these accounts are not renamed, they could be vulnerable if an intruder attempted to gain access by guessing the administrator password through a brute force attack.

The majority of accounts reviewed on the PDC had what appeared to be the user's last four (4) digits of their social security number associated with the account. If an account identifier is required, then something other than the user's social security number should be used.

If the agency's password policy is not enforced, an unauthorized user could easily obtain access to the accounts established on a machine.

Intruders often use inactive accounts to break into a network. If an account has not been used for a reasonable period of time, the account should be disabled until it is needed. This minimizes the possibility that an unauthorized user will access the account. An account should be deleted if it is not going to be reinstated. Further, default administrator, guest, and anonymous accounts in operating system and applications are some of the first accounts that an intruder will attempt to use. Therefore, they should be assigned strong passwords or, if possible, renamed or removed immediately after installation.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING: 04-CFC2-2: The Cabinet For Families And Children Should Ensure All Inactive Accounts Are Eliminated And That All Account Names Are Ambiguous (Continued)

Recommendation

We recommend CFC take the following actions:

- Default administrator accounts should be renamed to something more ambiguous in order to prevent unauthorized access.
- All accounts on all machines should be reviewed to determine which accounts have not changed their password within the last 31 days. These accounts should be evaluated to determine if they are still valid accounts that are required for a business-related purpose. If not, the accounts should be disabled or deleted depending on the necessity of reinstatement of the account.
- Personal information, including social security numbers, should not be used to identify an account.

Management's Response and Corrective Action Plan

We cannot turn off enumeration on the NT4.0 domain controllers as it would interfere with our normal operations. We can however address this problem on our other servers, but on an NT server setting "restrictanonymous" to 1 in the registry is largely ineffective as it still allows enumeration. This will be a moot point when we migrate to the AD domain. We are willing to rename the Administrator accounts on critical machines, but since we cannot prevent enumeration (on any domain controllers or NT4.0 machines) it is still possible to identify administrator accounts with little difficulty. We understand the criticality of purging dormant user accounts and will take steps to both monitor and purge unused/unnecessary user accounts on a scheduled basis. While there may be a minimal security risk to using the last four digits of a social security number this has been the one way in which we can confirm user identity. The last four digits, coupled with a procedure for calling the user back at their work place minimizes the possibility of a security compromise. We will address a possible replacement for the "last four" method but, as this method is deeply ingrained in our system, any change would take several months to implement.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-CWD1-3: The Division Of Unemployment Insurance Should Strengthen Controls Over Systematic Programs To Ensure Accurate Information Is Available For Closing Package Reporting

State Organization: Cabinet for Workforce Development

The agency has made several improvements in reporting the delinquent employer contribution receivables on the closing package. However, during testing of 45 delinquent employer contribution receivables and 45 deferred revenues, we discovered the following errors:

- Reports and/or payments were posted to an incorrect account and were not properly corrected during the audit process.
- Payments were received and not automatically applied to the outstanding balance on Program 42. This resulted in accounts receivable and accounts payable balances appearing in the system simultaneously for the same account at 6/30/04.
- Wages, excess wages, and taxable wages were scanned incorrectly on Program 42, which created a receivable. The errors were not caught during the audit process.
- In some instances journal entries were performed incorrectly or lacked proper supporting documentation to determine the cause for the adjustment (i.e. employer amended wages, etc.).
- Overpayments established over 5 years ago were still in the system and reported as deferred revenue. Information supporting the balance has been purged and cannot be verified.
- Receivable or deferred revenue amounts reported at 6/30/04 were not supported in the system when testing. The agency lacked adequate supporting documentation to explain these discrepancies.

Incorrect account balances results in an overstatement of receivables from delinquent employer contributions and deferred revenue on the closing package forms submitted to Finance for financial reporting purposes. An adjustment to decrease the accounts receivable balance in the amount of \$10,173,699 was reported to and made by Finance.

Proper internal control dictates that the agency should have a computer system in place to adequately maintain employer accounts to ensure that information input into the system is accurate and reliable.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-CWD1-3: The Division Of Unemployment Insurance Should Strengthen Controls Over Systematic Programs To Ensure Accurate Information Is Available For Closing Package Reporting (Continued)

Generally Accepted Accounting Principles (GAAP) dictates that government funds recognize revenues in the accounting period in which they become susceptible to accrual – both measurable and available. Therefore, amounts that are available, but not otherwise measurable, should be reported as deferred revenues rather than as revenue.

Recommendation

During testing this year, we noted areas of improvement from the prior year audit. However, there are several areas that still need to be addressed. Computer system and staff controls should be enhanced to ensure proper reporting of the closing package forms for financial statement purposes. Controls should be enhanced to prevent the reoccurrence of errors that affect the employer accounts.

Management's Response and Corrective Action Plan

As was noted there are improvements. We continue to train staff and make maintenance and programming changes as needed to address IT issue. We believe these efforts will continue to improve employer account receivable and payable balances.

- There are instances where payments are posted erroneously, and indeed this is one of the conditions we attempt to identify and correct in our report audit process. We are making efforts to ensure that the audit process is completed prior to the closing package. Continued training of staff should decrease these errors.*
- We agree that there are instances where payments that should have been automatically applied to an existing receivable were not correctly applied. We will investigate this and attempt to correct through training. Where programming "bugs" are identified we will request that COT correct the problem.*
- An outside vendor scans wages, excess wages and taxable wages. It is difficult for us to detect and correct incorrectly scanned wages, excess wages and taxable wages. We believe this to be an isolated incident.*
- Again, the finding of erroneous journal entries is being addressed through additional staff training and edits in the audit process.*

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-CWD1-3: The Division Of Unemployment Insurance Should Strengthen Controls Over Systematic Programs To Ensure Accurate Information Is Available For Closing Package Reporting (Continued)

Management's Response and Corrective Action Plan (Continued)

- *When preparing this years closing package we will not include deferred revenue amounts over five 5 years old.*
- *There are some instances where supporting documentation is lacking. We continue to stress to staff to adequately describe the reason for journal entries in the "Comment" section as well as having documents imaged that will support corrections.*

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-CWD2-4: The Division Of Unemployment Insurance Should Implement Controls To Ensure Proper Review Of Closing Package Forms Submitted To Finance And Administration Cabinet

State Organization: Cabinet for Workforce Development

For FY 04, CWD prepared closing package forms and submitted them to Finance And Administration Cabinet (FAC) without adequate review. As a result of the inadequate review the issues below were noted:

Accounts Payable:

During the accounts payable audit, the auditor noted that the estimated benefits payable to claimants included new year money due to a formula error. Further, the total population used to calculate the accounts payable estimate could not be verified to supporting documentation. Therefore, the agency had to revert back to the prior year methodology in estimating the amounts payable to claimants and submits an amended closing package for a second time. The auditor also noted the estimate for payments to other States accounted for the IRS withholding payments twice. This was brought to the agency's attention in the prior year audit; however, the total check register payments and the withholding amounts were used to calculate the FY 2004 estimate.

Accounts Receivable:

During the accounts receivable audit, the auditor noted several errors on the closing package. The errors included:

- Benefit overpayment receivables did not include penalties and interest;
- The allowance for uncollectibles equaled prior year actual write-offs and was not calculated based on the methodology documented;
- Other state receivables within 30 days included charges for the 6/30/04 quarter, which is not billed until July; and
- Several mathematical errors were noted, which were brought to the agency's attention in the prior year audit to prevent future errors. The agency submitted an amended closing package; however, some of the others were still not corrected.

Closing Package:

The agency submitted a final amended closing package; however, several errors were still noted. The errors included:

- A transposition of a number during the calculation of employer tax receivables within 30 days;

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-CWD2-4: The Division Of Unemployment Insurance Should Implement Controls To Ensure Proper Review Of Closing Package Forms Submitted To Finance And Administration Cabinet (Continued)

- The actual write-offs used to determine the allowance for uncollectibles for benefit overpayments did not agree to the Federal ETA 227 report for FY 03 and FY 04; and
- Several other mathematical errors were noted.

The numerous errors noted in the closing package created erroneous financial statement amounts and required several revisions on behalf of FAC and CWD.

Good internal controls dictate that adequate review procedures should be in place to ensure that the closing package contains verifiable and accurate data before submission.

Recommendation

We recommend that CWD implement controls to ensure that the closing packages are prepared consistently and accurately before submission. We also recommend that the information reported on the closing package be properly supported and verifiable.

Management's Response and Corrective Action Plan

- *Changes have been implemented to assure the closing packages submitted are inclusive of accurate calculations. The closing packages will be verified for accuracy prior to submission.*
- *Penalty and Interest was added to the amended report dated 9/27/04.*
- *Other states' receivables will be used for bills over 30 days old.*

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-CWD3-5: The Cabinet For Workforce Development Should Strengthen Controls Over The Processing Of The Unemployment Insurance Claimant Overpayments

State Organization: Cabinet for Workforce Development

While testing the Accounts Receivable closing package, the auditor identified weaknesses within the UI Claimant Overpayment process:

- The auditor noted lien fees processed from Fund 1200 are received in Fund 6200. These fees are not reimbursed to Fund 1200 and have not been for several years. The agency did go back to FY 2000 in an attempt to see what was owed to fund 1200.
- No action has been taken by CWD on a prior year verbal comment relating to the way in which the agency calculates interest on overpayments. Interest for the overpayment is simply calculated based upon the principal overpayment amount, not the principal amount plus any accrued interest at that date.

As a result of the above findings:

- Fund 1200 does not recoup their monies paid out on lien fees even after the claimant has paid back their overpayment, including the fee. This creates an understatement for fund 1200 and an over statement in fund 6200 of receipts.
- As a result of the miscalculation of interest, this represents a loss in interest that is earned and due to the agency when they do not properly charge the claimant.

KRS 341.415 (5) states, “In the event benefits have been paid as a result of false statement, misrepresentation, or concealment of material information by a recipient of benefits and have not been repaid by the recipient within one (1) calendar year from the date of the first notice, interest at the rate of one and five-tenths percent (1.5%) per month or any part thereof, shall be imposed on and added to the unpaid balance each successive month, providing due notice has been given to the recipient. Such interest shall be paid into the unemployment compensation administration account.”

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-CWD3-5: The Cabinet For Workforce Development Should Strengthen Controls Over The Processing Of the Unemployment Insurance Claimant Overpayments (Continued)

Recommendation

We recommend the agency implement controls to ensure all monies received are properly posted to the appropriate fund.

We recommend the agency further investigate the program responsible for calculating the interest on overpayments and update the software to ensure the agency is receiving all interest due them from claimants that have an overpayment account.

Management's Response and Corrective Action Plan

The Benefit Payment Control Section has provided the Trust Fund Officer with the lien fee information from 7/99. A journal voucher was processed on 10/04 to move the money to the correct account 1200. This process is now being done monthly. Programming is in process to calculate interest on the total amount of overpayment including interest. This should be in place for the closing package FY 2005.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-FAC1-6: The Finance And Administration Cabinet Should Develop And Implement A Formal Policy To Govern Security Of The Management Administrative And Reporting System Interface Files

State Organization: Finance and Administration Cabinet

As was noted during the previous year, the Finance and Administration Cabinet (FAC) has not developed or implemented a formal policy concerning security governing MARS Interface Files. Specifically, these procedures should cover the segregation of duties between development of checkwriter datasets and request for processing the datasets to create payments through MARS. Our review revealed 21 users with update access to one or more of 26 specific checkwriter files also had authorization to request these files be processed through Finance.

Allowing users the ability to update checkwriter files and authorize their processing increases the likelihood of unauthorized processing of checkwriter payments, and may compromise the integrity of data processed through MARS.

Formal policies provide a security framework to educate management and users of their security responsibilities. Consistent application of formalized security policy and procedures provides continuity for implementation and sets the tone of management concern for strong system security. To help ensure strong security and the integrity of checkwriter files, it is necessary to develop and implement a formal policy identifying management and user responsibilities concerning MARS checkwriter files. Further, the level of system access granted to users should be restricted to only areas necessary for an employee to perform assigned job duties. It is ultimately the responsibility of FAC to ensure that access to MARS interface files is reasonable.

Recommendation

We recommend that the Finance and Administration Cabinet develop and implement a documented formal policy to govern the security surrounding MARS interface files. This effort should include standardizing procedures to be implemented on a regular basis. We further recommend these procedures include steps to provide for a higher level of confidence in proper segregation of duties concerning update and processing of checkwriter files.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

**FINDING 04-FAC1-6: The Finance And Administration Cabinet Should Develop
And Implement A Formal Policy To Govern Security Of The Management
Administrative And Reporting System Interface Files (Continued)**

Management's Response and Corrective Action Plan

The Office of the Controller will develop and implement a formal policy governing the security access pertaining to checkwriter datasets. This policy will cover the segregation of duties in agencies between submission of checkwriter datasets and the request for processing the datasets to create payments through MARS.

The Office of the Controller will monitor users with "update" access to submit the datasets and confirm they are not authorized to submit the authorization request (E-mail), as well.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-FAC2-7: The Office Of Financial Management Should Implement Procedures To Ensure The Data Provided For The Year-End Investment Income Accrual Is Accurate And Complete

State Organization: Finance and Administration Cabinet

During our review of the FY 04 investment income accrual, we noticed discrepancies between the income and accrued earnings reported in the June month-end file used for the year-end accrual and the income and accrued earnings for June that was provided to us earlier for a different section of the audit. Upon further investigation, it was discovered that the file sent to Finance for the year-end accrual was not the final year-end file for June 2004 but was an incorrect, earlier version of the month-end file.

The investment income receivable in the original file was \$26,792,266. The actual investment income receivable, however, was \$6,785,215. By sending Finance the wrong file, the year-end investment income receivable was overstated by \$20,007,051. After allocating this balance among the investment pool participants, it would have come very close in materially misstating the revenues and investment income receivable for the Capital Projects Fund.

Good internal controls dictate that records be properly maintained and that information provided to other departments for accounting and financial reporting purposes be reviewed for accuracy and completeness.

Recommendation

Prior to sending Finance the file for the year-end investment income accrual, the Portfolio Manager should review and approve the file to ensure that it is correct. Although it is beneficial to maintain multiple copies of the Month-End files to provide a trail and supporting documentation for changes made between the initial file and the final file, final versions of the Month-End file should be kept separate from the earlier versions in the Library.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-FAC2-7: The Office Of Financial Management Should Implement Procedures To Ensure The Data Provided For The Year-End Investment Income Accrual Is Accurate And Complete (Continued)

Management's Response and Corrective Action Plan

We agree that we should have the final program in a separate file from the preliminary programs. The Office of Financial Management is currently working on a new program that will eliminate the need for multiple month end files. It is anticipated the new program will be in production or running parallel by July 1, 2005. Until the new programs are in production, OFM agrees to maintain preliminary copies of the month end files in a separate location from the final month end. In addition, OFM agrees to have the Accounting Supervisor review the year-end accrual information for accuracy/completeness prior to it being sent to Finance for inclusion in fiscal year end reporting.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-FAC3-8: The Finance And Administration Cabinet Should Ensure All Agencies Conduct Accurate And Timely Fixed Asset Inventory Counts

State Organization: Finance and Administration Cabinet

We observed fixed assets inventory counts at several agencies including Dept of Parks, Administrative Office of the Courts (AOC), and Cabinet for Workforce Development (CWD). The following weaknesses were noted:

Department of Parks:

While the physical inventory count procedures were improved over last year, the Department of Parks still had deficiencies using the results of the inventory count to correct inventory records in MARS. At four of the fourteen parks we audited, we noted that the results of the inventory counts were not reflected in MARS.

Administrative Office of the Courts:

The Administrative Office of the Courts had a significant delay in providing auditors and Finance and Administration Cabinet (FAC) with a corrected copy of the inventory record, which hindered the completion of audit work. While the inventory counts were conducted in May 2004, the corrected inventory report was not received until October 2004.

Cabinet for Workforce Development:

The physical inventory procedures were not satisfactory at either of the two CWD locations that auditors attended and did not follow FAC procedures. The inventory-taker ignored assets that were missing property tags. We also noted that several tagged items were missing from the MARS report. The inventory-taker speculated that these items were purchased and tagged, but not entered into the MARS system. One asset still in use was recorded in MARS as “surplus.” Further, the results of the inventory count were not used to correct inventory records in MARS.

Good internal controls dictate that a consistent set of procedures be followed when conducting a physical inventory count. This includes applying the results of the inventory count to correct fixed assets inventory records in MARS. Since FAC procedures were not followed, FAC cannot be certain that the fixed asset records used to compile the information for the Comprehensive Annual Financial Report are correctly stated.

KRS 45.313 states, “Each budget unit shall maintain a current inventory of equipment having an original cost of five hundred dollars (\$500) or more. The inventory shall be available for examination by the Finance and Administration Cabinet at all times.”

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-FAC3-8: The Finance And Administration Cabinet Should Ensure All Agencies Conduct Accurate And Timely Fixed Asset Inventory Counts (Continued)

The Finance and Administration Cabinet, Division of Statewide Accounting Services requires an annual physical inventory of fixed assets by all state agencies. FAC provides a Physical Inventory Procedures Manual for conducting the annual physical inventory. This manual provides details of how to conduct the fixed assets inventory count.

Recommendation

We recommend that FAC require agencies to conduct an annual inventory count of fixed assets following the policies and procedures outlined in the Finance and Administration Cabinet's Physical Inventory Procedures Manual. This would include using the 5003 Fixed Assets report to record the results of the inventory observation; searching for and adding unrecorded fixed assets; verifying and correcting the tag number, description, location, serial number, agency, organization and asset type for each asset; and making every effort to locate missing items. This would also include making appropriate, timely changes to the MARS inventory system to reflect the results of the physical inventory count and submitting the corrected 5003 report timely.

Management's Response and Corrective Action Plan

We concur with the audit finding. Agencies have been reminded to follow Statewide Accounting Services procedures for physical inventory observations. Additionally, agencies have been made aware of the weaknesses noted by the Auditors of Public Accounts and supplied a web link to the procedure document.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-FAC4-9: The Finance And Administration Cabinet Should Formalize And Consistently Apply The Program Modification Process For The Commonwealth's Cash And Investments System

State Organization: Finance and Administration Cabinet

During the audit of the controls over the Commonwealth's Cash and Investments System, it was discovered that the Office of Financial Management (OFM) has a program modification process in place; however, this process had not been formalized in standards or procedure statements specific to the agency. Further, as has been reported for the last two years, although agency personnel are aware of the program modification process, it is not being consistently applied to new programs development and changes to existing programs.

To help standardize the program modification process, OFM has developed a program modification request form called a Program Change Request (PCR). Among the steps associated with this form, approvals are required from various members of agency personnel to ensure that the requested change is necessary, the proposed coding change is reasonable, and the altered program code has been sufficiently tested for accuracy and applicability to the requested change. Once all of these approvals have been placed on the PCR, then a final approval to move the change into production must be applied.

The review of documentation maintained in support of the program modification process revealed that there was no central repository or logging of PCR requests that are within this program modification process. The auditor found 14 complete PCR requests and 2 incomplete PCR requests for changes that had been promoted to production within the possession of one or more of these individuals: the programmer, the internal auditor, and the librarian for the production environment. Also, after asking about new program development, there was an additional complete PCR form presented to the auditor, which had not been in the possession of any of these individuals during the testing phase.

During testing for FY 2004, the auditor identified 1,042 instances where changes were made within 36 programs. Of these changes, there were 254 instances, or 24.4 percent, that were not supported by a PCR or considered a 'general maintenance' change. Additionally, there were two instances of changes attributed to a PCR that did not go through the entire PCR process and another two instances associated with only an e-mail request.

As discussed with the agency during the prior year audit, a 'general maintenance' PCR may be used for routine program changes, which can include changes to the cycle number, fiscal year, date, number of days in the month, and file name changes where the

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-FAC4-9: The Finance And Administration Cabinet Should Formalize And Consistently Apply The Program Modification Process For The Commonwealth's Cash And Investments System (Continued)

file name contains a date or month that corresponds to the date/month being processed. There were 628 'general maintenance' changes identified within the 1,042 instances of changes for FY 2004, or 60.3 percent, that the auditor would consider meeting the requirements of a general maintenance program change.

Only one of these changes was supported by an e-mail requesting the change. The remaining 627 changes were not supported by an e-mail or other communication of the issues to be resolved, a code comparison identifying all changes made to the program, or proper approval from a person other than the programmer to move the changes into production.

A review of the PCR forms and supporting documentation revealed that there is no listing consistently developed that specifically discusses or shows the changes that were made in the program code. Of the 15 complete PCR forms for FY 2004, the auditor found only 3 forms, or 20.0 percent, whose supporting documentation included a code comparison between the original code and the revised code. For the remaining requests, the auditor was only able to trace changes based on the descriptions on the form of the proposed changes.

It was also discovered during this review of the complete PCR forms that there were a significant number of changes being placed into the production environment before receiving the final approval for implementation. There were a total of 12 PCR forms that were found in exception, or 80.0 percent of all complete PCR forms. Two forms were for changes that were moved to production before receiving the final approval for implementation, while another ten forms were for changes that were moved to production even before testing was reviewed and, of course, prior to any final approval for implementation. The most blatant example of this situation occurred when a program was placed in production nearly a month prior to the approval to proceed with changes and over seven months prior to the approval for implementation. This particular request concerned an initiative by OFM to modify existing programs and develop any necessary new programs to ensure that the cash within the portfolio accounts could be matched between the Commonwealth's financial system and the Cash & Investments System.

During discussions with the librarian over the production environment, it was discovered that due to a lack of documentation required, program changes could be placed into production without proper approval for implementation. Agency personnel had informed the librarian that the only requirement for uploading programs into the production

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-FAC4-9: The Finance And Administration Cabinet Should Formalize And Consistently Apply The Program Modification Process For The Commonwealth's Cash And Investments System (Continued)

environment was an e-mail message from the programmer. Further, the librarian does not participate in the completion of the PCR form, although there is a section on the form that is to be filled out by the person that has implemented the change to production.

Without a formalized program modification process and monitoring of the compliance with the process, the agency is at risk that procedures that are deemed vital to the process will be overlooked. For example, disregarding the procedure established to review supporting documentation for evidence that a change has been tested and approved for promotion to production could circumvent the control in place that only allows the librarian to have write access to the production environment. This increases the likelihood that unauthorized or inappropriate program changes could be placed into production.

The program modification process should be formalized, distributed, and understood by all applicable agency personnel. This process should be consistently applied to all code changes to existing programs and the development of new programs. Within the agency's response to FY 2003 comments, they showed their agreement with this criterion by stating, "All new programs and modifications to programs must have a program change form filled out."

To ensure that all program modifications are monitored and thoroughly documented, a procedure should be established for logging all program modification requests and a standard should be developed to define the supporting documentation to be maintained with the PCR form.

Recommendation

We recommend that OFM formalize, implement, and consistently apply control procedures over the program modification process. Specifically, the agency should, at a minimum:

- Develop a formal procedure manual for the program modification process. This manual should include the procedures to adequately document program specifications and understanding of program objectives, to specifically identify changes in code by developing a code comparison listing between the original code and the revised code, to properly

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-FAC4-9: The Finance And Administration Cabinet Should Formalize And Consistently Apply The Program Modification Process For The Commonwealth's Cash And Investments System (Continued)

Recommendation (Continued)

complete the PCR form, to adequately test proposed program code changes, and to verify that all approvals are in place for the program code change before implementation to the production environment.

- Process all new programs and modifications to existing programs through the established program modification process as documented in the formal procedure manual.
- Ensure all changes comply with established program modification procedural requirements. Requirements should include that an individual other than the programmer properly reviews all changes for accuracy and that proper approvals are documented authorizing implementation of the change into production before the librarian moves the change to the production environment. After implementation of changes, the librarian should sign and date the PCR form to affirm that this process has been completed.
- Ensure, for those changes that relate to a 'general maintenance' PCR form, that the programmer provides supporting documentation for the request of the program changes, inclusive of an e-mail or other communication of the issues to be resolved, identification of the specific program code that was changed to satisfy the request, and approval from a person other than the programmer to move the changes into production. All personnel involved with authorizations on the PCR form should be made aware of the responsibilities they are assuming with their authorizations on these forms.
- Establish a logging feature within the program modification process. This log should include the name of the originator, origination date, brief description of problem, programs affected, completion date, and implementation date.
- Establish a centralized location for maintaining all complete PCR forms.

We are aware that the agency has begun the process to replace the current Cash and Investments System; however, we believe that the recommendations proposed are universal enough to relate easily with the new system development. It is the historical precedent within OFM to require continuous program changes that has caused the auditors to strongly advocate the agency formalize and consistently apply appropriate program change control procedures.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-FAC4-9: The Finance And Administration Cabinet Should Formalize And Consistently Apply The Program Modification Process For The Commonwealth's Cash And Investments System (Continued)

Management's Response and Corrective Action Plan

The Office of Financial Management agrees the Program Change Request is not being completed as required. We are currently in the process of writing a new program. This will eliminate the need to make any updates to the old SAS program. Once the new program is in place, all program files will be placed in the Library. Any change to the file will require approval of the Accounting/IT supervisor. The Librarian will be instructed to move the files after the supervisor has approved. Once the new program is complete, a formalized process for program changes will be completed and implemented. The new month end program will run through LanBatch, therefore the program changes will not be implemented until approved by the supervisor and moved to the Library.

We will establish a logging procedure for program change requests and have one documentation file that will have all signed reports.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-FAC5-10: The Finance And Administration Cabinet Should Strengthen Logical Security Procedures Surrounding The Complete Assets Management Reporting and Accounting System

State Organization: Finance and Administration Cabinet

During the FY 2004 audit of the Commonwealth's Cash and Investments System, the Office of Financial Management (OFM) did not properly secure the critical financial data associated with the distribution of earnings from investments. Further, OFM has not developed or implemented a formalized security policy that identifies management and user responsibilities concerning IT security surrounding the Cash and Investments System.

By moving all production programs into a secured file directory that is restricted to the Librarian and the Commonwealth Office of Technology administrators, OFM has increased the security over the system programs. However, the auditors found a significant number of files, including production data files, being used within current system programs that reside in another directory that is not as strictly secured. Also within this directory is the staging libraries used by the programmer to hold programs waiting to be moved to production. All OFM staff currently has 'Change' access to these files, which would allow them to read, add, alter, or delete these files.

Without strong, formalized, logical security controls, the opportunity increases for unauthorized modification to production files as well as the likelihood of errors or losses occurring from incorrect use of data and other resources.

Formalized security policies set the tone of management concern for strong system security and provide a security framework used to educate management and users on their responsibilities. Further, access to directories that house programs and critical financial data should be restricted to only necessary employees. System security should be administered in such a way as to ensure proper segregation of duties. Granting users system access that would allow the ability to alter or delete programs or financial data prior to or subsequent to processing increases the risk of financial misstatements or fraudulent reporting.

Recommendation

We recommend that OFM develop and implement a formalized security policy that standardizes security responsibilities for all employees and ensures critical programs and data are properly secured. All Cash and Investment System related

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-FAC5-10: The Finance And Administration Cabinet Should Strengthen Logical Security Procedures Surrounding The Complete Assets Management Reporting and Accounting System (Continued)

Recommendation (Continued)

programs should be reviewed to ensure that financial data files being used or created are being housed in a properly secured directory. Further, access to the program staging library should be properly restricted.

Management's Response and Corrective Action Plan

A formalized policy will be written and implemented during FY2006. We are in the process of writing a new program and the security policy will reflect that program. Beginning with FY2006, all program files will be maintained in the Library. The only time the files will be moved/changed is when a program change request has been submitted and approved. After the programmer makes the change, the files will be placed in a secure folder. The folder will have security to allow only the supervisor to have write access. Once the files have been reviewed and approved by the supervisor the Librarian will be contacted to move the files into the Library.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-PARKS1-11: The Department Of Parks Should Improve Controls Over Timesheets And Payroll Reports

State Organization: Department of Parks

During payroll testing at the Department of Parks, we examined a sample of 25 Parks employees' personnel records, timesheets and timecards for several attributes. The results of our testing included the following exceptions:

- An employee's compensatory time was not added to his leave balance. This was corrected during testing.
- An employee took sick leave but no request for leave was present.
- An employee worked overtime but no overtime request form was present.
- An employee's timecard from one state park could not be located. However after additional searching the employee's timecard was found. The following exceptions were noted for this timecard. This employee's working hours and overtime hours were overstated. We requested his timecards for three more pay periods. One timecard shows incorrect working hours. The working hours were overstated. The hours he took for sick leave were more than what he should have taken. His overtime hours were overstated in the payroll worksheet.

Failure to add compensatory earned on the leave balance would show an inaccurate leave balance. Failure to present leave forms or overtime request would not show evidence of approval. Failure to ensure that working hours are calculated correctly on timecards would show incorrect numbers in the Uniform Payroll and Personnel System (UPPS). Employees would be paid incorrectly.

Kentucky Administrative Regulation (101 KAR 2:034 Section 7(3)) states an employee who is eligible for overtime shall request permission from or be directed in advance by the supervisor to work overtime.

Kentucky Administrative Regulation (101 KAR 2:102 Section 2(5)) states an employee shall file a written application for sick leave with or without pay within a reasonable time.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-PARKS1-11: The Department Of Parks Should Improve Controls Over Timesheets And Payroll Reports (Continued)

In addition, good internal controls dictate that timesheet/timecards and supporting forms should be reviewed to prevent errors in recording payroll.

Recommendation

We recommend the following:

- A request for overtime should be submitted by each employee prior to any overtime worked.
- Leave forms should be submitted to obtain approval if leave is taken.
- Timesheets, timecards, leave requests, overtime requests and reports should be examined more closely to prevent errors in payroll. They should be maintained centrally and easily located.

Management's Response and Corrective Action Plan

We agree with your recommendations. The first 2 are procedures that are in place and we feel these are isolated incident. But, it is important that they be complied to. So, we will remind everyone that overtime and leave requires prior approval and written documentation.

As to the last comment concerning the lost timecard, this park went through 3 payroll officers in 18 months. The Payroll Manager of the Central Office has discussed in great detail the importance for them to keep more accurate records in the future.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-REV1-12: The Department Of Revenue Should Ensure All Sales And Use Tax Returns Are Processed Accurately And Reconciled Monthly And All System Changes Are Adequately Tested

State Organization: Department of Revenue

Our audit revealed that Department of Revenue (Revenue) data entry, program code and system design problems resulted in the Department of Technology, Systems Support Branch's failure to successfully reconcile actual Sales and Use Tax processed control totals to the statistical database control totals for the months of September 2003 through January 2004. Although some corrective action has been taken to prevent additional errors, adequate controls were not established to identify and correct certain data entry errors and there is still an unexplained discrepancy of \$989. Our review revealed that testing of program changes performed prior to implementation of the new Sales and Use Tax – Electronic Escrow system did not include all possible transaction types, which allowed these system errors to occur.

The Sales and Use Tax - Electronic Escrow system was implemented in October 2003 to ensure taxpayers only receive a bill for the total amount due minus all payments made on the return, even if their payments were submitted separate from the return. After returns are posted to a transaction database, the program matches Sales and Use Tax payments that come in without a return (204 payments) to returns received without a payment (transaction code 12 – no pay return). If a match is found, the return leaves escrow, is processed, and is posted to the master and statistical databases. If a match is not found the transaction is held in escrow and not posted.

Systems Support performs a monthly reconciliation of the Sales and Use Tax activity. For the months of September 2003 through January 2004 there was a total \$59,606 in discrepancies between the Sales and Use Tax processed control totals per the statistical database and the actual total processed for the months. Of this amount, \$34,208 is attributed to transactions being held in escrow, as the partial payments could not be matched to an associated return. Also, in November a data entry error of \$18,463 was identified during reconciliation, but this transaction was reversed in December during processing to fully correct this out of balance figure.

The following issues were noted for the remaining \$6,935.

Seven transactions totaling \$3,825 were attributed to a problem with the program code. A program glitch inappropriately changed transactions that should have been coded with

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-REV1-12: The Department Of Revenue Should Ensure All Sales And Use Tax Returns Are Processed Accurately And Reconciled Monthly And All System Changes Are Adequately Tested (Continued)

a pay code of '2' (a part-pay) to a pay code of '3' (a 204 payment) indicating that the return was received without a payment. Additionally in attempting to obtain the total amount paid on partially paid returns, returns were being held and the amount paid fields were manipulated to reflect all monies that had come in with the return plus any additional monies that had been posted to the master database. In instances where an additional payment was not found on the master database the amount paid field was being changed to \$0.00, instead of adding zero for the additional payments to the partial payment amount sent in with the return. These transactions did not post to the master or statistical database. These discrepancies have been corrected with seven (7) one-side journal vouchers to post the payments to the appropriate taxpayer's account on both the statistical and master databases.

Four (4) transactions totaling \$2,121 were attributed to a design problem. All transactions were matched to an account and posted to the master database REVSU01. Revenue then coded the part-pay transactions with a pay code of '3' (indicating a 204 payment) not realizing that this pay code would prevent the transaction from posting to the statistical database. The transaction was then returned to the transaction database (REVSU08) for processing. Sales and Use tax processing extracts transactions from the transaction database and updates the master and statistical databases with transactions that have not previously been processed. This measure was intended to prevent payment postings from being duplicated. Since the master database had already been updated with the four transactions, the statistical database was not updated with the partial payments during processing. Because of the Escrow Project Team's uncertainty of the effect of making adjustments to these accounts, no adjustments were made to the statistical and/or master database. The design problem was remedied by removing partial payments from the Electronic Escrow process on December 29, 2003.

One (1) of the four (4) transactions was a \$1,000 payment on an account with an original amount due of \$5,077. Previously, two (2) separate \$1,000 payments were made on the account for a total of \$3,000 paid, making the new amount due \$2,077.

The payment kicked out of the system with an error code of '028' - underpayment of \$1,000 or more. Additionally, as a result of the pay code being erroneously changed to a '3', as discussed above, the error report reflected a code of '138' (204 payment) instead of '128' (part-pay). This resulted in the \$1,000 payment sent in with the return to reflect the total of \$3,000 that had been paid on the account. The compliance section staff member working the report added the two (2) \$1,000 payments previously made (but

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-REV1-12: The Department Of Revenue Should Ensure All Sales And Use Tax Returns Are Processed Accurately And Reconciled Monthly And All System Changes Are Adequately Tested (Continued)

already included in the \$3,000) to account for all three (3) payments. This duplicated the \$2,000 in credits to the taxpayer's account, erroneously bringing the amount paid to \$5,000 and the new amount due to \$77.

Compensating controls were not in place to identify or correct this type of error and/or alert compliance section staff of the duplicated payments. This error was not addressed until it was noted during the auditor's follow-up on this out of balance transaction on 11-03-2004. A tax due notice for this account dated 11-04-2004 was issued to correctly reflect the outstanding balance plus any applicable penalties and interest.

January 2004, there was a balancing discrepancy of \$989 that could not be attributed to part-pay returns. Neither the Systems Support Branch nor the Electronic Escrow Project team could provide an explanation for this outstanding discrepancy.

Additionally the Systems Support Branch provided the auditor with incomplete supporting documents for the balancing discrepancies in October and November. Supporting documentation was provided to the Systems Support Branch, by the Electronic Escrow Project team prematurely and did not include an explanation for all out of balance amounts for these months and resolution. This information was not made available to the Systems Support Branch until it was provided to the auditor during fieldwork. Subsequently, updated copies were forwarded to Systems Support branch staff to include with monthly balancing work papers.

Without consideration of all possible scenarios during the system design and testing phase management increases the risk of developing and implementing systems that involve inefficient, ineffective, and/or inaccurate processing of data. The design of newly developed systems and function of associated program code may be fallible. The integrity of the data processed through the Sales and Use Electronic Escrow system may be questioned when balancing discrepancies exist as a result of inadequate system design and testing procedures, or the lack of controls governing the identification and resolution of errors.

System design and testing controls should ensure that newly developed systems function properly. Accurate balancing of the monthly Sales and Use Tax worksheets will ensure that all taxpayer accounts are credited properly. All out of balance amounts must be researched to determine the cause of any discrepancy and a required resolution. The applicable Revenue staff should develop and maintain documentation of errors and their eventual resolution.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-REV1-12: The Department Of Revenue Should Ensure All Sales And Use Tax Returns Are Processed Accurately And Reconciled Monthly And All System Changes Are Adequately Tested (Continued)

Recommendation

We recommend Revenue staff in conjunction with the Electronic Escrow Tax Project team:

- Ensure testing of new systems or system changes are adequate to prevent loss of data, or require time and effort to investigate issues that arise following implementation. System testing should include all possible scenarios and types of applicable tax returns/payments.
- Ensure adequate documentation is prepared to explain any out of balance amounts and include this documentation with the monthly reconciliation support.
- Develop controls that will ensure transaction error codes are accurately applied.
- Determine the cause of the \$989 amount that was outstanding for the month of January 2004, document and resolve appropriately.

Management's Response and Corrective Action Plan

The Department of Revenue takes very seriously the responsibility of testing new systems or system changes. An effort was made to try to include all possible scenarios when the Electronic Escrow Tax Project was tested. However, sometimes due to process changes, human error, etc., not every possible combination can be tested for. Systems cannot always be built to handle exemptions but should be built to handle the normal processing of returns and payments. The Department will make every effort to ensure testing on future systems or system enhancements will be as thorough as possible. Time and effort will be devoted to investigate issues arising from the new system and to finding a solution.

Documentation will be prepared for out of balance issues in future.

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FINDING 04-REV1-12: The Department Of Revenue Should Ensure All Sales And Use Tax Returns Are Processed Accurately And Reconciled Monthly And All System Changes Are Adequately Tested (Continued)

Management's Response and Corrective Action Plan (Continued)

If the above recommendation was referring to the below issue, then it should be noted that a production cut over was completed on 11/07/03 to remedy the situation and this should not occur in the future.

The payment kicked out of the system with an error code of '028' - underpayment of \$1,000 or more. Additionally, as a result of the pay code being erroneously changed to a '3', as discussed above, the error report reflected a code of '138' (204 payment) instead of '128' (part-pay). This resulted in the \$1,000 payment sent in with the return to reflect the total of \$3,000 that had been paid on the account. The compliance section staff member working the report added the two \$1,000 payments previously made (but already included in the \$3,000) to account for all three payments. This duplicated the \$2,000 in credits to the taxpayer's account, erroneously bringing the amount paid to \$5,000 and the new amount due to \$77.

Compensating controls were not in place to identify or correct this type of error and/or alert compliance section staff of the duplicated payments. This error was not addressed until it was noted during the auditor's follow-up on this out of balance transaction on 11-03-2004. A tax due notice for this account dated 11-04-2004 was issued to correctly reflect the outstanding balance plus any applicable penalties and interest.

While staff was unable to resolve the January out of balance, they had identified a production problem and were able to correct it. The production fix was cutover on 12/29/03. After January, no further out of balance issues have been noted in the process. If more information becomes available that would enable us to produce a report on the January out of balance issue, then we would document that information as we did for the other months that had an out of balance issue.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-TC1-13: The Transportation Cabinet Should Improve Inventory Procedures for Maintenance Materials

State Agency: Transportation Cabinet

The Transportation Cabinet (TC) has maintenance barns in each of the 12 districts throughout Kentucky. For FY 04, TC had \$25.3 million worth of inventory on their balance sheet. Our auditors observed district personnel conduct their inventory to determine if maintenance materials were counted correctly and to determine if inventory management procedures were adequate.

Several inconsistencies were noted. Some sites had complete guardrail systems on their lot and did not count them with their inventory, while others did. These guardrail systems appear to be leftovers from construction projects. In 4 counties we observed, the guardrail systems and remnants totaled approximately \$5,775.

Items such as antifreeze, oil, grease, etc were included on the OMS inventory sheets used by district personnel in conducting their inventory. District personnel were unclear as to whether they were responsible for counting those items or not because those are usually included with the Equipment Division inventory. In the 4 counties observed, items such as antifreeze, oil and grease totaled \$3,756.

There were several instances where the observers had written in additions on the OMS inventory sheets, however, these additions were not made by the record keepers.

There are no policies and procedures in place to instruct district maintenance personnel on inventory procedures. Record keepers do not have a clear understanding of OMS and have not been adequately trained.

Statement 1, paragraph 73 of the National Council of Governmental Accounting (NCGA) requires “significant amounts of governmental fund inventories to be reported in the fund balance sheet.” Such a requirement makes it imperative to have accurate counts of inventory.

Recommendation

We recommend TC develop policies and procedures for inventory observations. These policies and procedures should cover items such as what to do with leftover construction project materials as well as responsibilities of each division. Record keepers should be adequately trained on using the OMS system. There were several new timekeepers who expressed their desire and need for OMS training.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-TC1-13: The Transportation Cabinet Should Improve Inventory Procedures for Maintenance Materials (Continued)

Management's Response and Corrective Action Plan

The Kentucky Transportation Cabinet (KTC) has developed a Policies and Procedures manual for OMS Material inventory and for inventory observations. This manual was revised and updated in March 2005. While each inventory item is not specifically mentioned, there is a policy outlined for all materials in the inventory. This includes salvaged guardrail components and items received from the Equipment garages or the central office Equipment Warehouse. The revised manuals are being sent to each district for distribution to all administrative units. In response to training needs, when the OMS system was implemented, all OMS administrative units were given extensive training. The OMS training team is committed to providing training to any administrative unit requesting training. We feel the procedures in place during the inventory process were meeting the objective of National Council of Governmental Accounting criteria requiring "significant amounts of governmental fund inventories to be reported in the fund balance sheet."

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-TC2-14: The Transportation Cabinet Should Implement Procedures To Ensure An Accurate Conversion Of Data To New Systems

State Organization: Transportation Cabinet

The Department of Bridge Inspections maintains its information in two (2) separate software programs located on two (2) different servers. The authoritative source for bridge information is the National Bridge Information System (NBIS), which is housed on a mainframe computer. However, the department also maintains its own data in the Kentucky Bridge Information System (KBIS), which is in development and is housed on a Windows NT server. Per discussion with TC management, this is only temporary; eventually, KBIS will become the authoritative source for bridge information.

This type of situation increases the possibility for errors and discrepancies.

During the process of developing and implementing a new system that is replacing a current system, procedures should be established to ensure the complete and accurate conversion of current system data to the new system.

Recommendation

We recommend that department management ensure KBIS implementation procedures include a procedure to perform a thorough comparison of all data in NBIS and KBIS to ensure the completeness and accuracy of data housed within the new KBIS system.

Management's Response and Corrective Action Plan

FY 03 Response:

The Division of Operations Bridge Inspection Section still maintains its information in two separate software programs the National Bridge Information System (NBIS) that is housed on a mainframe computer, and the Kentucky Bridge Information System (KBIS) that is housed on a Windows 2000 server. This is only being done temporarily and that eventually KBIS will become the authoritative source for bridge information. During this temporary stage, which is almost final stage, we have always been successful in making sure no errors occur. We are making sure of the completeness and accuracy of bridge inspection and inventory

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

**FINDING 04-TC2-14: The Transportation Cabinet Should Implement Procedures
To Ensure An Accurate Conversion Of Data To New Systems (Continued)**

Management's Response and Corrective Action Plan (Continued)

FY 03 Response (Continued):

data during on-going collection and input activities. We are hoping by July 2004 the KBIS will be implemented, and the KBIS will be part of Kentucky Bridge Maintenance system (KYBMS) software in future so that NBIS that resides on the mainframe will no longer exist.

FY 04 Response:

The Division of Operations Bridge Management Branch purchased the KYBMS system to replace the KBIS system several years ago. Both systems are being maintained until Operations personnel are assured the new system will meet their need to evaluate the status of bridges maintenance needs. This has been a slow process due mostly to employee turnover in the affected branch. Currently a new staff member has been assigned the task of evaluating and utilizing the KYBMS system.

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(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-TC3-15: The Transportation Cabinet Should Implement Procedures To Ensure The Integrity Of The Highway Information System Database

State Organization: Transportation Cabinet

The Highway Information System (HIS) maintains data on bridges, as well as all other public roads in the state. The information contained in the HIS database is collected and maintained by various TC divisions. The integrity of the HIS data is dependent upon both the accuracy and frequency with which the data is updated and the users interpretation. It was noted in the prior year audit that there is no time schedule for updating that data. The source of the bridge information is kept on the NBIS server. The Department of Bridge Inspections maintains this data. Per current discussion with management, we noted that it has been several months since the HIS server had downloaded the latest information from NBIS and that no new processes have been implemented to compare the data contained in the HIS server with that contained in the NBIS server.

The agency has stated this was due to a scheduled replacement of NBIS. To date, no additional procedures have been performed to ensure that HIS data has been updated from the current KBIS data. The agency expects to upgrade HIS in the first half of 2004 to actually implement a direct link to KBIS information for HIS users and eliminate the need for KBIS downloads into HIS.

When information regarding bridges is not updated periodically, the various divisions within the TC do not have the most recent information for analysis purposes. Specifically, it is important for the Division of Planning, which uses that data in HIS, to have current and reviewed information regarding bridges.

Data integrity control procedures should be established that are adequate to ensure the integrity of the data maintained within the organization's databases. Procedures should be established to ensure that data used by management remains complete, accurate and valid during its input, update, and storage. Further, data elements should be balanced periodically to the control records or master files in the case of data interfaces.

Recommendation

Procedures should be implemented that ensure the integrity and completeness of bridge information provided to HIS users. Until the direct link between HIS and KBIS information is completed, we recommend a current download from KBIS to HIS be performed and data be refreshed at least on a quarterly basis.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
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(CONTINUED)**

SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-TC3-15: The Transportation Cabinet Should Implement Procedures To Ensure The Integrity Of The Highway Information System Database (Continued)

Management's Response and Corrective Action Plan

FY 03 Response:

We would like to re-emphasize that bridge data is maintained and available from the Traffic & Operations Division. KBIS is the official source file for reporting and/or analysis.

As stated last August, our goal is to establish a link between the KBIS and HIS systems. We are currently developing a process to download bridge information from KBIS, including the new unique bridge id, to the existing HIS system. As the HIS upgrade progresses, this download will assist us in our design and plan for a potential link, and will aid the Traffic & Operations Division with improving bridge locations.

Our schedule for upgrading the HIS system to Highways by Exor includes a production load of existing data for evaluation by June 30th of this year, and running in parallel with the current system until it is determined that the upgrade successfully meets the Cabinet's reporting and analysis requirements.

FY 04 Response:

The Division of Planning uses the Highway Information System (HIS) system to maintain the inventory of all Transportation Highway Infrastructure. To track bridges there has been an effort to link the HIS system to the Bridge Maintenance System (BMS) in order to ensure accurate tracking of all bridges. This linking of data has been delayed due to the implementation of a new HIS system (developed by Exor) which upgrades the HIS system to a new platform to accommodate the Cabinet wide enterprise system. The Division of Operations inability to implement the new KYBIS system that replaces the KBIS system (mentioned in number 3 above) also consternates the resolution of this condition.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-TC4-16: The Transportation Cabinet Should Improve Data Retention Practices

State Organization: Transportation Cabinet

Our examinations of the data retention for information maintained within the NBIS and within the Pavement Management System (Visual/PMS) revealed that year-end downloads are not kept for these databases. Information contained in the Required Supplementary Information includes prior year data. Additionally, trend analysis often requires detailed information for prior year data that may not have been included in a separate report.

Failure to retain year-end downloads means there is no practical method to determine or test the records and their corresponding field data for prior years.

Electronic data that provides support for financials included within the annual report should be retained in a manner similar to that required for non-electronic support. This data should be retained as provided for in an approved retention schedule with the Kentucky Department of Library and Archives. Master files and electronic data that is considered necessary for an audit trail should be retained as long as necessary for audit purposes.

Recommendation

We recommend the TC ensure they retain year-end downloads for the NBIS and Visual/PMS databases in order to facilitate and substantiate prior year reporting, as well as to provide a detailed backup that can be tested for accuracy in the event clarification is needed. If upgrades to these systems have been or will be implemented, then the TC should ensure the same considerations for data retention are included in the implementation.

Management's Response and Corrective Action Plan

FY 03 Response:

A Bridge Management System (BMS) and a Pavement Management System (PMS) have been selected for implementation, but these systems have not been fully implemented. The pavement management data and the Bridge Inventory data at present is stored on the mainframe with back-up of the data as per GOT's policy and procedures for backing up data. Data entered in the selected Visual BMS and PMS has a date/time and user stamp in the database. Therefore, the changes

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-TC4-16: The Transportation Cabinet Should Improve Data Retention Practices (Continued)

Management's Response and Corrective Action Plan (Continued)

FY 03 Response (Continued):

in the data can be tracked. All prior year data is available to do trends analysis. With the full implementation of these two systems in the next one to two years, the stated weakness will cease to exist.

FY 04 Response:

The Division of Operations is still working to implement the changes detailed in the response to the auditors FY 03 finding. Operations is running dual systems at this time and with some minor computer program modifications will be ready to cut over to the new software. The target date for completion is by the end of Fiscal Year 2005. As recommended by the Auditor's Office, the new software will track data changes and the user making the changes as recommended by the Auditors.

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-TC5-17: The Transportation Cabinet Should Improve Audit Trail Procedures For Database Actions

State Organization: Transportation Cabinet

Adequate audit trails were not implemented for various databases within the TC. Our examination of internal controls over infrastructure assets revealed that no reports are currently generated by the TC that show the data attribute changes, records added, and records deleted. In addition, some databases do not contain a field for when the date information was entered or a field identifying the user performing the data entry.

In order to properly track potential data entry errors or other errors in the database, it is important to know when the entry error occurred and the identity of the individual making the entry.

Without adequate audit trails, it is difficult or impossible to determine the exact timing, source, and cause of database data entry errors or unauthorized changes to records. It may also result in the inability to properly recover data in the case of some errors.

Adequate audit trails should be provided to facilitate the tracing of transaction processing and the reconciliation of disputed data. Accounting systems and database management systems should include an audit trail component that includes sufficient information, such as the terminal device or microcomputer involved, user identification codes, data field affected, and time and date entries. The TC's system development life cycle methodology should include procedures requiring that each information system development or modification project have adequate audit trails specified.

Recommendation

We suggest the TC consider adding fields to provide sufficient audit trails of database alterations or security violations, including the date entered and entry person for all changes to the critical databases. In addition, we believe the TC should consider generating a nightly report showing all changes to the database that were made each day.

Management's Response and Corrective Action Plan

FY 03 Response:

During analysis of the Land & Buildings database/application, new requirements were uncovered which kept increasing the scope of the project; some of the

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

FINDING 04-TC5-17: The Transportation Cabinet Should Improve Audit Trail Procedures For Database Actions (Continued)

Management's Response and Corrective Action Plan (Continued)

FY 03 Response (Continued):

requirements also [would have] generated policy and process changes. Effectively, because of other priorities and setbacks, the effort waned. At this time, we are making a minimum number of changes to the database and system in an effort to comply with the intent of the recommendations. These changes are expected to be complete by the end of this month.

Further remediation efforts and/or a possible rewrite of a lands & building inventory system need to be at the direction of the system user/owner - Division of Property and Supply Services. Likewise, further responses to issues surrounding this system should likely be coordinated through the Division of Property and Supply Services.

FY 04 Response:

Asset tracking for the Cabinet is achieved on 4 separate platforms. These systems are very diverse in nature and the solution offered by the auditor's office does not apply to all of these systems.

- A) Vehicles are tracked with the OMS system and the inventory controls are an intricate part of this system. It was developed by a third party and does not contain the tracking of changes suggested by the Auditor's Office. It does a very good job of maintaining the assignment, billing and recovery of cost for the Cabinet. There are no plans at this time to modify this system to track changes to vehicle inventory.*
- B) Office & Lab Equipment is tracked using the MARS statewide system which also does not track changes to the system as outlined by the auditors.*
- C) Lots & Building are tracked using a Dbase III application. This system has just been upgraded by the Division of Technology and should fully meet the expectations of the Auditor's Office.*
- D) Computer Equipment & Software is tracked on a Dbase III application. This software doesn't address the auditor's recommendations and there are no plans to modify the application now used. It does however meet the needs of the Division of Technology for their computer tracking needs.*

There is a preliminary study to replace systems B, C & D with a software package named Archibus. This system is an integrated package that inventories and tracks

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SECTION 2 – FINANCIAL STATEMENT FINDINGS

**FINDING 04-TC5-17: The Transportation Cabinet Should Improve Audit Trail
Procedures For Database Actions (Continued)**

Management's Response and Corrective Action Plan (Continued)

FY 04 Response (Continued):

Lots, Buildings and their contents. It is currently in use by the Finance and Administration Cabinet Real Property Section and we could possibly become a part of a statewide system.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

***Reportable Conditions Relating to Internal Controls and/or Reportable
Instances of Noncompliance:***

**FINDING: 04-CFC6-18: The Cabinet For Families And Children Should Maintain
Case File Records That Include Client Applications, Recertifications, And Records
Of Eligibility Determinations**

State Agency: Cabinet For Families And Children

Federal Program: CFDA 93.558 – Temporary Assistance For Needy Families

Federal Agency: U.S. Department for Health and Human Services

Pass-Through Agency: Not Applicable

Compliance Area: Eligibility

Amount of Questioned Costs: \$18,224

We reviewed 77 TANF cases for eligibility and of the cases reviewed, seven (7) cases (or 9%) could not be located or produced by one (1) Division of Community Based Services (DCBS) local office. In addition, while performing Lifetime Limit testing, another case file could not be located from another DCBS local office, bringing the total missing case files to eight (8), which resulted in \$18,224 of questioned costs.

This has been an ongoing problem and the agency has not taken appropriate action to address this internal control weakness.

When TANF case files and records are not maintained or cannot be located, we cannot review client information and documentation for TANF eligibility. In addition, if local DCBS offices do not maintain adequate case records, CFC and the United States Department of Health and Human Services (DHHS) cannot be assured that benefits are issued to eligible recipients.

Federal Regulations at 45 CFR 205.60(a) state,

The State agency will maintain or supervise the maintenance of records necessary for the proper and efficient operation of the plan, including records regarding applications, determination of eligibility, the provision of financial assistance...The records will include information concerning the date of application and the date and basis of its disposition; facts essential to the determination of initial and continuing eligibility (including the individual's social security number, need for, and provision of financial assistance); and the basis for discontinuing assistance.

**COMMONWEALTH OF KENTUCKY
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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-CFC6-18: The Cabinet For Families And Children Should Maintain Case File Records That Include Client Applications, Recertifications, And Records Of Eligibility Determinations (Continued)

Federal Regulations at 45 CFR 92.42(b)(1) also state, "...records must be retained for three years from the starting date specified in paragraph (c)...."

Recommendation

As recommended last year, case files should be maintained to adequately support applications, eligibility determinations, case decisions, and expenditures. CFC should work with local offices (including Fayette County) to assist them in developing and maintaining an adequate filing system so that case files can be tracked and located. Since one local county office has had missing case files in the past two audits, CFC could consider having that local office store files in a central location and require caseworkers to sign out and return cases to the central filing location periodically. In addition, CFC could consider assigning someone the responsibility of keeping track of the case files and maintaining the central file room so that this control weakness can be corrected.

Management's Response and Corrective Action Plan

As a result of the Cabinet being cited for this issue in previous audits, the Cabinet worked with Fayette County to implement a new filing system in the local office. Staff from the Division of Family Support went to Fayette County last year for three (3) months to assist in organizing their case files as part of the Cabinet's corrective action plan. The corrective action plan consisted of obtaining a case listing, assign cases to workers based on the alphabet, then have the workers keep those files in their offices. Also, the discontinued case files were to be maintained to allow a worker easy access when someone reapplied.

The corrective action plan was implemented. However, due to high staff turnover in the office, it appears problems are arising when trying to redistribute cases as a result of a worker leaving. The Cabinet will work with Fayette County to assure the local office is following the corrective action plan and implement procedures to follow when a caseload needs to be redistributed. Additionally, the Cabinet will monitor their progress and assist in addressing any problems as they arise.

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(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-CFC7-19: The Cabinet For Families And Children Should Maintain Adequate Records To Ensure Payments Are Made For Approved And Allowable Goods And Services To Eligible Recipients

State Agency: Cabinet For Families And Children

Federal Program: CFDA 93.558 – Temporary Assistance For Needy Families

Federal Agency: U.S. Department for Health and Human Services

Pass-Through Agency: Not Applicable

Compliance Area: Activities Allowed/Unallowed and Eligibility

Amount of Questioned Costs: \$16,774

We tested a sample of 77 TANF cases from DCBS offices in eight (8) counties. Local offices failed to produce records to support expenditures and follow procedures outlined in Volume III – *Kentucky Transitional Assistance Program (K-TAP)* and Volume IIIA – *Kentucky Works Program (KWP)* of CFC’s operating manual.

We noted problems in the following areas, which resulted in \$16,774 of questioned costs:

- Several K-TAP and KWP payments were issued inappropriately (six (6) of 77 cases, 7.8% deficiency rate, \$1,232 questioned cost).
- Four (4) K-TAP cases (or 5.2% of those tested) were assigned a new recertification period of one (1) year in error as a result a caseworker making a change (such as an address change) on the client’s account. Likewise, two (2) Kinship Care applications/recertifications were processed yet, other than one (1) Kinship Care Rights and Responsibilities form for one (1) case, evidence could not be produced to document that the client came in for recertification (six (6) of 77 cases, 7.8% deficiency rate, \$3,432 questioned cost).
- Several problems were noted with tracking or following up on KWP compliance and sending out the *KW-204 Conciliation Contact* forms timely (six (6) of 77 cases, 7.8% deficiency rate, \$1,865 questioned cost).
- Birth records for two (2) children (who were likely born out of state) could not be produced (one (1) of 77 cases, 1.3% deficiency rate, \$5,400 questioned cost).
- Social Security number and/or the date and year of birth of the client’s child were entered incorrectly into the system for two (2) cases (two (2) of 77 cases, 2.6% deficiency rate).
- Several Public Assistance form PA-32s problems were noted, including
 - forms processed with unused lines not crossed out in the “Description of item or service to be provided” section of the form (nine (9) instances),
 - forms were issued stating they were valid for 30 days when the policy manual states the forms are only valid for 10 days (three (3) instances), and

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-CFC7-19: The Cabinet For Families And Children Should Maintain Adequate Records To Ensure Payments Are Made For Approved And Allowable Goods And Services To Eligible Recipients (Continued)

- one PA-32 form was not used for a car repair, which resulted a client receiving a \$500 payment based upon a car repair estimate and not an actual invoice (one (1) instance).
- A form PA-33 could not be located to support transportation payments and three (3) transportation payments were issued from one (1) PA-33 (three (3) of 77 cases, 3.9% deficiency rate, \$120 questioned cost).
- Problems were noted with obtaining and responding to Household and School Verifications (four (4) of 77 cases, 5.2% deficiency rate, \$4,725 questioned cost).
- Problems were noted with requesting, utilizing, and updating the system for the PAFS-700 Verification of Income form (four (4) of 77 cases, 5.2% deficiency rate).
- Numerous problems were noted with other K-TAP and KWP forms, including the PA-219, Transitional Assistance Agreement, CS-333, KIM-101, KIP-106, KIM-125, PAFS-14, and the PA-85 (41 of 77 cases, 53.2% deficiency rate).

Some of these (or similar) items were commented on in the FY 01, FY 02, and FY 03 audits, yet CFC has not taken adequate measures to correct these problems.

There are numerous effects of the above weaknesses. In general, when K-TAP and KWP policies and procedures are not adhered to, CFC cannot be assured that expenditures are being made appropriately and K-TAP payments could be made to ineligible individuals. This could result in DHHS assessing a penalty against CFC. According to 45 CFR 262.1(a)(1), the penalty could be for “the amount by which a State misused its TANF funds.”

Good internal controls dictate that when caseworkers make expenditures of Federal awards, the client’s eligibility determination should be reviewed adequately and completely to ensure only eligible participants receive Federal funding. Good internal controls also dictate that program personnel be adequately trained and supervised to ensure Federal monies are expended appropriately in accordance with program policies and procedures.

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(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-CFC7-19: The Cabinet For Families And Children Should Maintain Adequate Records To Ensure Payments Are Made For Approved And Allowable Goods And Services To Eligible Recipients (Continued)

Federal Regulations at 45 CFR 205.60(a) state,

The State agency will maintain or supervise the maintenance of records necessary for the proper and efficient operation of the plan, including records regarding applications, determination of eligibility, the provision of financial assistance. The records will include information concerning the date of application and the date and basis of its disposition; facts essential to the determination of initial and continuing eligibility (including the individual's social security number, need for, and provision of financial assistance); and the basis for discontinuing assistance.

Recommendation

In general, we recommend K-TAP policies and procedures be adhered to prior to making expenditures of Federal awards. In addition, CFC should consider increasing management and quality control reviews of K-TAP applications, recertifications, and payments to ensure they are made appropriately in accordance with policies and procedures.

Last year, we noted problems in specific counties and responses to the comment were provided only from those counties; however, we recommended CFC provide caseworkers statewide with a reminder on the specific problems found in the FY 03 audit. These problems in the K-TAP and KWP programs continued during FY 04 and based upon the evidence obtained from the cases sampled in various counties, we do not believe they are isolated to a few DCBS offices but are indicative of problems occurring statewide. Therefore, we recommend that the management response be provided at Cabinet level so that these items can be addressed adequately throughout the state.

Management's Response and Corrective Action Plan

The Cabinet for Health and Family Services realizes its responsibility in ensuring each case is processed timely and accurately. The processing of cases correctly prevents and reduces the potential for fraud and administrative errors.

The Cabinet utilizes various forms of communication to inform field staff of policies and procedures of case management. These forms of communication include Kentucky Works Program (KWP) Tips, KAMES News Messages, Family Support Memorandums (FSM), Operations Manual Updates (OMU) and

**COMMONWEALTH OF KENTUCKY
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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-CFC7-19: The Cabinet For Families And Children Should Maintain Adequate Records To Ensure Payments Are Made For Approved And Allowable Goods And Services To Eligible Recipients (Continued)

Management's Response and Corrective Action Plan (Continued)

Operations Manual Transmittal Letters (OMTL). OMUs and OMTLs are distributed to provide policy updates and revisions made to the operations manuals. FSMs are distributed to provide clarification of procedures. KWP Tips and KAMES News Messages are posted directly to KAMES. Because they are posted on KAMES, they are available to everyone who has access, which includes field staff and also training. This is the quickest and most efficient manner to communicate with field staff. KWP Tips are reminders to field staff of best practices, procedures, and policy for case managers to utilize in their performance of providing benefits and services to the clients. KAMES News Messages allows us to inform field staff when there may be systems problems, checks being mailed late, etc. The Cabinet will use these methods to address specific problems that were identified in this audit.

It was recommended in the audit for the Cabinet to increase management and quality control reviews. The Cabinet has already increased the number of cases that are to be reviewed by quality control. This number was increased from 1000 cases a year to 1020. The way the sample is taken was also changed to ensure a representative sample of cases is pulled from each region. A proposal has been made to include K-TAP eligibility in quality control reviews and increase even further the number of cases to be reviewed. This proposal is currently in the office of the Commissioner for the Department for Community Based Services awaiting a decision.

The Cabinet is currently in the process of phasing in a new program called State On-Line Query (SOLQ) System. SOLQ will be used to match social security numbers (SSN), birth dates, and names of individuals with information from the Social Security Administration. This process will be incorporated into KAMES processing at the following actions at member level: Applications at case and member level; all member adds for recertifications, program transfer, and case change; SSN change; and special circumstance. The SOLQ transaction date and case information will be captured and stored. From this date, reports for auditing purposes will be created. SOLQ is another avenue to assisting in the accuracy of data entered into KAMES.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
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(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-CFC7-19: The Cabinet For Families And Children Should Maintain Adequate Records To Ensure Payments Are Made For Approved And Allowable Goods And Services To Eligible Recipients (Continued)

Management's Response and Corrective Action Plan (Continued)

The PA-32, Authorization for Supportive Services Payments, is used to verify expenses and authorize payments for items and services associated in the Kentucky Works Program and education or training. The policy stated in the audit is incorrect. The PA-32 is valid for 30 calendar days after issuance. However, the participant only has 10 days to present the form to the provider. If the form is presented within days, then the provider has until the end of the 30-day period to return the form for payment. If the form is not presented to the provider until after 10 days, the form is no longer valid and the client must request a new form. Policy is contained in Vol. IIIA, MS 5360 and in the procedural instructions for the form. Policy and proper use of the form will be reinforced to field staff.

Beginning February 2005, the Cabinet began collecting overpayments as a result of administrative errors. It is the Cabinet's desire that reinstituting this policy will motivate workers to process cases timely and accurately. If they do not, it will add to their workload, as it is their responsibility to establish the claim. Additionally, the cabinet is going to propose the collection of supportive services. This will be a creation of new policy to be implemented by the Cabinet.

The Cabinet is unsure as to why a new certification period was assigned to cases when making a case change. The Cabinet will research this issue to determine if it is a systems issue or caseworker error. If it is a systems issue, a request will be made to fix the problem. If it is a caseworker error, the Cabinet will issue a KAMES News Message, as well as an e-mail to program specialists, service region administrators and service region administrator associates to address the problem.

Using the recommendations made in the audit, the Cabinet will address the specific issues itemized in the audit on a statewide level. As we are able to identify specific cases, these will be presented to the regions to have correct policy and procedures addressed with the case managers.

Furthermore, by strengthening monitoring, implementing SOLQ, and creating new policy, the Cabinet hopes to create more accountability by the worker thus reducing worker error.

**COMMONWEALTH OF KENTUCKY
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(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-CFC8-20: The Cabinet For Families and Children Should Only Issue Work Incentive Payments To Eligible Individuals And Should Request And Maintain Adequate Documentation Of The Eligibility Determinations

State Agency: Cabinet For Families And Children

Federal Program: CFDA 93.558 – Temporary Assistance For Needy Families

Federal Agency: U.S. Department for Health and Human Services

Pass-Through Agency: Not Applicable

Compliance Area: Eligibility

Amount of Questioned Costs: \$1,040

During the FY 04 TANF Eligibility testing, we reviewed six (6) Work Incentive (WIN) payments and each of these payments had deficiencies. While testing other payments, we noted an additional WIN deficiency and it is discussed below as well. During testing, we reviewed the WIN-1 *Work Incentive (WIN) Report* for seven (7) clients and we noted the following, which resulted in \$1,040 of questioned costs:

- 1) WIN payment was issued to the client even though they responded their income exceeded the gross income limit for their family size and attached check stubs that demonstrated this as well. (two (2) of seven (7) cases – 28.6% deficiency rate)
- 2) WIN payment was issued to a client even though the client responded that their gross income exceeded the threshold for their family size. A check stub detailing income for the period was not attached. Evidence could not be produced by the local office to show that the caseworker contacted the client to verify their income eligibility/ineligibility. (one (1) of seven (7) cases – 14.3% deficiency rate)
- 3) WIN payment was issued to the client even though check stubs or proof of employment were not submitted. (one (1) of seven (7) cases – 14.3% deficiency rate)
- 4) WIN payment was issued without the client's response to the gross income question and check stubs were not submitted. Given the client's employment as a teacher and the family status, it is likely the gross income exceeded the limit for the family size. (one (1) of seven (7) cases – 14.3% deficiency rate)
- 5) WIN payment was issued to the client and a copy of the supporting WIN-1 form could not be produced (one (1) of seven (7) cases – 14.3% deficiency rate).
- 6) WIN payments were issued to the client when the client responded that they did not have work expenses and evidence that the case worker contacted the client to explain the WIN requirements and verify the work expense response could not be produced. (four (4) of seven (7) cases – 57.1%)

When WIN payment policies and procedures are not adhered to, TANF payments could be made to ineligible individuals. This could result in DHHS assessing a penalty against CFC.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-CFC8-20: The Cabinet For Families and Children Should Only Issue Work Incentive Payments To Eligible Individuals And Should Request And Maintain Adequate Documentation Of The Eligibility Determinations (Continued)

- 1) According to the WIN-1 form, clients are not eligible if gross income for their family size exceeds an established threshold. If the client states their income exceeds this threshold and also attaches supporting documentation that proves this, caseworkers should not issue a WIN payment.
- 2) Question #3 on Form WIN-1 asks, “Are you currently working? If yes, you must attach proof. This could be a check stub from the current month or a statement from your employer.” The form also states, “Remember....attach the necessary proof.”
- 3) See #2 above.
- 4) The Form WIN-1 should be filled out completely by the client. This form states, “Please read each question carefully and check your answer. Be sure to attach any necessary proof. If you have any questions about this form call your worker...Remember: Read and answer all questions carefully.”
- 5) Federal Regulations at 45 CFR 205.60(a) state,
The State agency will maintain or supervise the maintenance of records necessary for the proper and efficient operation of the plan, including records regarding applications, determination of eligibility, the provision of financial assistance...The records will include information concerning the date of application and the date and basis of its disposition; facts essential to the determination of initial and continuing eligibility (including the individual’s social security number, need for, and provision of financial assistance); and the basis for discontinuing assistance.
- 6) See # 4 above.

Recommendation

We recommend the following:

- 1) When clients respond that their income exceeds the gross income limit for their family size and attach check stubs that verify this, caseworkers should not issue a WIN payment, as the client is clearly ineligible.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
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(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-CFC8-20: The Cabinet For Families and Children Should Only Issue Work Incentive Payments To Eligible Individuals And Should Request And Maintain Adequate Documentation Of The Eligibility Determinations (Continued)

Recommendation (Continued)

- 2) When clients respond that their income exceeds the gross income limit for their family size but fail to attach proof of employment or a check stub, the caseworker should request check stubs for the month to ensure they are income eligible. The WIN-1 form states in two (2) places that clients are required to attach proof of eligibility. Caseworker actions should be documented in System Tracking For Employability Programs (STEP) and changes to the client's responses should be documented on the WIN-1 form by the caseworker.
- 3) When clients fail to attach proof of employment (check stub or statement from employer), either contact should be made with the client to request this information and the WIN-1 payment should be placed on hold until the information arrives or the WIN payment should not be made.
- 4) When clients fail to answer the gross income question but attach check stubs, caseworkers should take the time to review the stubs for income eligibility. If the caseworker does not have enough information to document that the client's income is below the threshold, contact should be made with the client and additional information requested. The WIN payment should either be put on hold until all of the information is obtained or the WIN payment should not be made.
- 5) WIN payments should not be made without supporting WIN forms. In addition, an adequate filing system should be maintained so forms and eligibility documents can be kept to support expenditures.
- 6) If the client responds that they do not have work expenses, either the WIN payment should be put on hold until clarification can be made or the WIN payment should not be made. If the caseworker believes the client misunderstood the meaning of "work expenses," they should contact the client to clarify the meaning and document the clients response both on the form and in the case comments in STEP. If clients do not have work expenses, a WIN payment should not be made.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-CFC8-20: The Cabinet For Families and Children Should Only Issue Work Incentive Payments To Eligible Individuals And Should Request And Maintain Adequate Documentation Of The Eligibility Determinations (Continued)

Recommendation (Continued)

When we presented the problems noted above to the case managers for their response, we were informed that the client's statement is accepted under many circumstances. Although we understand CFC does not want to overburden clients with documentation, if the WIN form states proof (such as a check stub or statement from the employer) must be attached, case managers should ensure the necessary proof is submitted prior to payment. Given the high deficiency rates noted, we recommend CFC implement policies and procedures to ensure WIN payments are only paid to clients who are eligible based upon their income. In addition, if adequate documentation is not obtained to support the expenditure, payment should not be made and actions should be documented more thoroughly in the case comments in STEP.

Since these problems were noted statewide and were not limited to one (1) particular county, response and action should be taken at the Cabinet level and not at the county level.

Management's Response and Corrective Action Plan

It is the Cabinet's response that adequate policies and procedures are in place to ensure payments are made only to eligible individuals. Vol. III, MS 3850 and MS 3860 outline eligibility criteria and procedures workers must follow to issue WIN payments. The errors cited in the audit were made by field staff.

The Cabinet will reinforce to field staff proper procedures that are to be followed when determining eligibility and processing payments for WIN. The Cabinet will inform field staff to review all supporting documentation for accuracy, completeness and eligibility prior to making payment.

Since the implementation of WIN, the Cabinet has had the ability to establish and collect claims as a result of agency error. Authority to allow the Cabinet to collect administrative error claims is provided in 921 Kentucky Administrative Regulation 2:520, Section 5.

**COMMONWEALTH OF KENTUCKY
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(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-CFC9-21: The Cabinet For Families And Children Should Document and Correctly Report Unliquidated Balances and Obligations on Quarterly Reports And Ensure Unliquidated Balances Are Spent Appropriately

State Agency: Cabinet For Families And Children

Federal Program: CFDA 93.558 – Temporary Assistance For Needy Families

Federal Agency: U.S. Department for Health and Human Services

Pass-Through Agency: Not Applicable

Compliance Area: Period of Availability

Amount of Questioned Costs: None

While performing the FY 04 TANF Period of Availability testing, we reviewed the Federal Fiscal Year 2003 ACF-196 *TANF Financial Report* for the quarter ended September 30th, 2003. Line 9 of this report lists \$44,068,271 of “Federal Unliquidated Obligations” and Line 10 reports an “Unobligated Balance” of \$8,490,818. We were unable to substantiate how the \$44,068,271 of “Federal Unliquidated Obligations” as reported on Line 9 was determined. Since this amount could not be verified, this means we were also unable to substantiate the \$8,490,818 “Unobligated Balance.” Since CFC could not produce documentation for how these amounts were arrived at and could not provide evidence that the “Unobligated Balance” was spent only on “assistance,” CFC was not in compliance with the TANF Period of Availability requirements for this grant.

If CFC does not spend “Unobligated Balances” on “assistance”, this could result in the DHHS assessing a penalty equal to the amount spent on non-assistance against CFC.

The compliance supplement requires “Unobligated balances from previous fiscal years may only be expended on benefits that meet the definition of assistance at 45 CFR section 260.31 and related administrative costs associated with providing such assistance.”

45 CFR 260.31(a)(1) states, “The term ‘assistance’ includes cash, payments, vouchers, and other forms of benefits designed to meet a family’s ongoing basic needs (i.e., for food, clothing shelter, utilities, household goods, personal care items, and general incidental expenses).” 45 CFR 260.31(a)(3) continues with, “Except where excluded under paragraph (b) of this section, it also includes supportive services such as transportation and child care provided to families who are not employed.” This section goes on to exclude “Supportive services such as child care and transportation provided to families who are employed,” therefore these are considered non-assistance expenditures.

According to 45 CFR 262.1(a)(1), “A penalty of the amount by which a State misused its TANF funds” could be assessed by DHHS.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-CFC9-21: The Cabinet For Families And Children Should Document and Correctly Report Unliquidated Balances and Obligations on Quarterly Reports And Ensure Unliquidated Balances Are Spent Appropriately (Continued)

Recommendation

Prior to year-end, we recommend CFC implement procedures to correctly report “Unliquidated Balances” and “Federal Unliquidated Obligations” on lines 9 and 10 of the ACF-196 report. Documentation for how these amounts are arrived at should be kept so that they can be reviewed for accuracy and compliance. In addition, we recommend CFC implement procedures to ensure and document that “Unliquidated Balances” are spent on items meeting the definition of “assistance”.

Management’s Response and Corrective Action Plan

The Cabinet agrees with the “Federal Unliquidated Obligations” and Unobligated Balance amounts reported on the ACF-196 report for quarter ending September 30, 2003. Prior to FY 05 the Cabinet reported Federal Unliquidated Obligations as the difference between award amount and expenditures based on all TANF award being budgeted. The Unliquidated Balance of \$8,490,818 was the result of a performance award the State of Kentucky received in addition to the original award. Since the performance award was in addition to the original award amount the \$8,490,818 was not budgeted and thus it was classified as Unobligated Balance on the report. Any unspent TANF funds at the close of a grant year can only be expended on benefits. With the project number change in Management Administrative and Reporting System at the beginning of each new grant year this directs all current expenditures to the new grant. Journal Voucher Corrections are manually processed moving benefit expenditures from the new grant to the old grant until all old TANF funds are expended. The reporting of Federal Unliquidated Obligations was changed at the request of the Atlanta Regional Office beginning FY 05. Only outstanding contract balances are reported as Federal Unliquidated Obligations.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CFC10-22: The Cabinet For Families And Children Should Improve Child Support Enforcement Performance To Ensure Children Receive Proper Financial Support

State Agency: Cabinet for Families and Children

Federal Program: CFDA 93.563 – Child Support Enforcement

Federal Agency: U.S. Department of Health and Human Services

Pass-Through Agency: Not Applicable

Compliance Area: Special Tests and Provisions

Amount of Questioned Costs: None

During FY 04 testing for Establishment of Paternity and Support Obligations, Enforcement of Support Obligations, Securing and Enforcing Medical Support Obligations, and Child Support Services for Interstate Cases, we found 12 of the 32 child support cases reviewed were out of compliance.

- In three (3) Medicaid cases, medical insurance was not ordered. The contracting official did not take any action to modify the order to include medical insurance.
- In three (3) Medicaid cases, medical insurance was ordered, but there was no documentation showing an attempt to obtain health insurance.
- In one (1) Medicaid and interstate case, medical insurance was ordered. The contracting official did not attempt to obtain medical support from the other state.
- In two (2) cases, medical insurance was ordered. The contracting official did not take any action to pursue medical support.
- In one (1) interstate case, the agency did not send out the Uniform Interstate Family Support Act petition or file criminal non-support charges.
- In one (1) case, the agency did not quarterly attempt to locate the non-custodial parent from February 1999 to February 2004 to establish paternity and support obligation.
- In two (2) cases, the non-custodial parents were employed during FY 04. Wage assignment was not issued to enforce the support obligations or arrears payoff.

Most of the deficiencies we noted above were lack of securing and enforcing medical support obligations. Some children without medical support obligations are covered under the Medicaid program. The Kentucky Medicaid program may be expending millions of dollars a year, which could be avoided if medical support orders were in place or enforced. House Bill 267 (2005 session) has language to strengthen this area.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CFC10-22: The Cabinet For Families And Children Should Improve Child Support Enforcement Performance To Ensure Children Receive Proper Financial Support

CFC is required to conduct self-reviews of its child support program. We compared our testing results to the State self-assessment's results for the compliance requirement of securing and enforcing medical support obligations. We noted the following deficiencies:

- The State's self-assessment did not show that all identified cases noted previously except for one case, were not in compliance for securing and enforcing medical support obligations.
- We requested the checklists for the self-assessment and found CFC did not keep all of checklists.
- CFC provided the contracting official the review sheets for cases found to be out-of-compliance but did not ask the contracting official to take any corrective action or provide a corrective action plan.

The effects of the weaknesses noted above include failing to:

- Take a timely action to establish or enforce obligations may not provide the proper service to children who need financial support.
- Order or enforce medical support may cost the Kentucky Medicaid program millions of dollars.
- Identify deficiencies during the self-assessment may not ensure the contracting office follows the regulations.
- Retain the checklists for self-assessment may not meet the Federal record retention requirements.
- Require the contracting official take corrective action or provide a corrective action plan may not ensure all objectives for providing child support services are met.

45 CFR Section 303.31 (b) states the IV-D agency shall:

- (1) Unless the custodial parent and child(ren) have satisfactory health insurance other than Medicaid, petition the court or administrative authority to include health insurance that is available to the noncustodial parent at reasonable cost in new or modified court or administrative orders for support.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CFC10-22: The Cabinet For Families And Children Should Improve Child Support Enforcement Performance To Ensure Children Receive Proper Financial Support (Continued)

(5) Provide the custodial parent with information pertaining to the health policy which has been secured for the dependent child(ren) pursuant to an order obtained under this section.

(6) Inform the Medicaid agency when a new or modified court or administrative order for child support includes medical support and provide the information . . . to the Medicaid agency when the information is available.

(7) If health insurance is available to the noncustodial parent at reasonable cost and has not been obtained at the time the order is entered, take steps to enforce the health insurance coverage required by the support order and provide the Medicaid agency with the information . . .

45 CFR section 92.42 (b)(1) states, "...records must be retained for three years"

Good internal controls dictate that deficiencies found from the self-assessment should be corrected or a corrective action plan should be provided.

Recommendation

We recommend the following:

- The contracting officials should use appropriate location sources to locate the non-custodial parent in a timely manner.
- The contracting officials should take the appropriate action to enforce the support obligation in a timely manner.
- For compliance with securing and enforcing medical support obligations,
 - In Medicaid cases, if an order exists and health insurance is not part of the order, the contracting official should seek modification of the order to include health insurance. The contracting official should inform Medicaid when a new or modified order includes medical support.
 - If health insurance is ordered, the contracting official should verify insurance information. In Medicaid cases, the insurance information should be sent to Medicaid.

COMMONWEALTH OF KENTUCKY
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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CFC10-22: The Cabinet For Families And Children Should Improve Child Support Enforcement Performance To Ensure Children Receive Proper Financial Support (Continued)

Recommendation (Continued)

- CFC should provide more training to its contracting officials to ensure all regulations and procedures are followed and required timeframes are met.
- CFC should provide training to field staff for conducting the self-assessment to ensure all compliance criteria are reviewed correctly.
- Checklists for the self-assessment should be maintained for three (3) years.
- CFC should ask the contracting official to take corrective action or provide a corrective action plan for out-of-compliance cases found during the self-assessment.

Management's Response and Corrective Action Plan

DCBS responses to the program compliance audit of the Kentucky Child Support Program for FY 04. Each recommendation is addressed separately.

The contracting officials should use appropriate location sources to locate the non-custodial parent in a timely matter.

Locate is not a criterion for the Federal Self-assessment, but the locate time frames may be reviewed in three (3) of the review criteria: establishment, enforcement and review and adjustment. The federal compliance standard for each of these categories is 75%. These criteria had 712 actions out-of-compliance, but only 9% of the actions were out-of-compliance for locate. Of the 32 cases reviewed in this audit, only one (1) case was out-of-compliance for locate. We do not believe the audit or the Federal Self-assessment identify locate as a major deficiency in meeting the federal requirements.

- *The contracting officials should take the appropriate action to enforce the support obligation in a timely matter.*

The compliance rate for the Enforcement Criteria for FY 04 was 75%, an increase of eight (8) percentage points over FY 03. Although the Federal compliance requirement of 75% was met for the Enforcement criteria, performance in this area needs to continue to improve. Program staff will continue to monitor Contracting Officials' performance and to work with the Contracting Officials to utilize system reports for monitoring and maintaining enforcement caseloads.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CFC10-22: The Cabinet For Families And Children Should Improve Child Support Enforcement Performance To Ensure Children Receive Proper Financial Support (Continued)

Management's Response and Corrective Action Plan (continued)

- *For compliance with securing and enforcing medical support obligations.*

-In Medicaid cases, if an order exists and health insurance is not ordered, the contracting official should seek modification of the order to include health insurance. The contracting official should inform the Medicaid agency when a new or modified order includes medical support.

-If health insurance is ordered, the contracting official should verify insurance information. The insurance information should be sent to the Medicaid agency in Medicaid cases.

We agree the Child Support Program continues to experience problems with establishing and enforcing medical support. Attached to this response is a corrective action plan for Medical Support Enforcement.

CFC should provide more training to its contracting officials to ensure all regulations and procedures are followed and required timeframes are met.

The Training Branch has a waiting list for scheduling training sessions from the existing curriculum. With upcoming changes, the Training Branch is committed to developing and conducting training in other areas. The Division of Child Support will issue manual material on the federal requirements, timeframes and the Federal Self-assessment. The manual material will be issued by August 1, 2005.

CFC should provide training to field staff for conducting self-assessment to ensure all compliance criteria are reviewed correctly.

We would like to note that this audit was conducted in only one (1) of 16 regions. FY 04 was the second year state field staff conducted the Federal Self-assessment reviews. This is a learning process, and we expect the case reviewers will become more proficient in the review process. When the sample for FY 05 is distributed, staff in the Division of Child Support will conduct a teleconference with the state field staff to go over the review method and to answer any questions.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CFC10-22: The Cabinet For Families And Children Should Improve Child Support Enforcement Performance To Ensure Children Receive Proper Financial Support (Continued)

Management's Response and Corrective Action Plan (Continued)

Checklists for the Self-assessment should be maintained for three (3) years.

We agree with this recommendation. A memorandum will be issued to staff.

CFC should ask the contracting official to take a corrective action or provide a corrective action plan for out-of-compliance cases found during the Self-assessment.

The purpose of the Federal Self-assessment is to give the states an opportunity to assess whether federal requirements for providing child support services are being met. It was designed as a tool to measure the state's compliance, not county compliance. The number of cases pulled for each county is based on the percent of the county caseload to the caseload in the Service Region. For most counties, enough cases are not reviewed in each category to constitute a valid sample for the county. As a result, the county compliance rate may not be correct, and more importantly, decisions could be made on invalid data. We do not concur with the recommendation to require a corrective action plan from contracting officials for failure to comply with the Federal Self-assessment. We believe the Federal Self-assessment alone cannot be used to determine a county's compliance with meeting federal requirements; however, the Self-assessment review can be used in conjunction with other contracting official performance reports to measure compliance.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CFC10-22: The Cabinet For Families And Children Should Improve Child Support Enforcement Performance To Ensure Children Receive Proper Financial Support (Continued)

Management's Response and Corrective Action Plan (Continued)

Department for Community Based Services

Corrective Action Plan

Division of Child Support

Performance Indicator: Medical Support Enforcement

<i>Task Item</i>	<i>Priority</i>	<i>Purpose</i>	<i>Actions to be taken</i>	<i>Due Date</i>
1	Issue Policy on Public Consulting Group (PCG) Project	Statewide implementation	Write policy document to notify staff of the PCG project and identify staff responsibilities.	3/15/2005
2	Statewide implementation of PCG Project	Identify existing medical ins. and issue notices to enroll Medicaid children in all counties	Task 1	3/15/2005
3	Upload MMIS Data in KASES	Update child support system with existing insurance and notify of lapse in coverage	Develop requirements, program and test changes to KASES.	6/1/2005
4	Create performance reports and monitoring reports for caseworkers	To measure performance and to assist workers in monitoring cases	Obtain report specifications for and review existing reports. Request enhancements or new reports. Program and test enhanced or new reports.	9/1/2005
5	Create a Web based Medical Support training session	Establish a resource to improve medical support enforcement	Develop the training curriculum.	9/1/2005
6	Create additional data elements for tracking	Report reliable data for federal reports	Change programming of the OCSE 157.	12/1/2005 This date is contingent upon the date the federal requirements are finalized.

**COMMONWEALTH OF KENTUCKY
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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-CFC10-22: The Cabinet For Families And Children Should Improve
Child Support Enforcement Performance To Ensure Children Receive Proper
Financial Support (Continued)**

Management's Response and Corrective Action Plan (Continued)

<i>Task Item</i>	<i>Priority</i>	<i>Purpose</i>	<i>Actions to be taken</i>	<i>Due Date</i>
7	Conduct training for all caseworkers	Enhance worker expertise in medical support enforcement	Establish Schedule. Monitor participation.	1/1/2006
8	Create Performance Measure for contracting officials	Provide incentive for improving performance	Add performance measure to the contract. Complete tasks 4 and 6.	7/1/2006

**COMMONWEALTH OF KENTUCKY
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(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CHS1-23: The Cabinet For Health Services Should Provide Better Safeguards For Funds Placed In Its Care

State Agency: Cabinet for Health Services

Federal Program: CFDA 93.778 – Medical Assistance Program

Federal Agency: U.S. Department of Health and Human Services

Pass-Through Agency: Not Applicable

Compliance Area: Allowable Costs

Amount of Questioned Costs: None

In previous years the APA has issued comments in the area of SMI for failing to reconcile agency reports against UNISYS reports to determine that valid claims were properly processed and paid. However, the agency has made an effort in the past year to resolve this issue and provide corrective action to include this control as part of administering the program.

However, during fieldwork of the fiscal year 2004 audit, and as part of the ongoing agency effort to reconcile system information, the APA became aware of a situation that caused the Department for Medicaid Services (DMS) to expend an approximate \$5,000,000 additional dollars for one month of premiums for Supplementary Medical Insurance (SMI). As a result of revised programming efforts, a large number of eligible participants were removed from the Medicaid roll, as well as, a number of ineligible participants being added to the Medicaid roll. DMS has made efforts to recoup any ineligible payments.

SMI payments made during fiscal year 2005 included:

July -	\$ 9,016,941
August -	\$ 8,749,306
September -	\$ 8,602,681
October -	\$14,129,211
November -	\$ 9,035,492
December -	\$ 7,351,565

A simple trend analysis of Medicaid payments made during fiscal year 2005 would have indicated a large spike in payments from September to October. Although performing such analysis may not be a necessary control feature, having done such an analysis may have prevented an error of this magnitude from occurring.

The APA is continuing review of this matter and will be coordinating additional audit work with federal agencies.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CHS1-23: The Cabinet For Health Services Should Provide Better Safeguards For Funds Placed In Its Care (Continued)

When the state overpays any bill by \$5 million questions must be asked to ensure the oversight agency is properly safeguarding the assets of the Commonwealth. During times of shortfalls and budget crisis even more emphasis must be placed on safeguarding and protecting every dollar. This problem is that the state spent money it did not need to spend.

The State should ensure through its financial internal controls that when invoice/premium payments jump by a large and/or unusual amount that those in higher positions in the cabinet are notified. Corrective action should be taken or at least attempted before issuing payments. We acknowledge this would be difficult for the DMS in this area since a refusal to pay would have cost thousands of citizens their health insurance, while the problem was resolved. However by attempting this they could have at least demonstrated that internal controls were operating as designed and effective.

Recommendation

The APA recommends that DMS as well as CHFS review its payment procedures so that large jumps in contract/premium amounts are not paid “just because that was the amount they sent me”. DMS and CHFS should ensure that every effort is made to not only secure the health and medical needs of the citizens of the Commonwealth but to secure their financial responsibility to the citizens.

Management’s Response and Corrective Action Plan:

Background:

At issue is the Kentucky Department for Medicaid Services’ (DMS) submission to the Centers for Medicare and Medicaid Services (CMS) of the DMS Buy-In Input file containing August 2004 accretion and deletion data. This file, which was submitted to CMS at the end of August 2004, was found to have contained erroneous data.

The data was contained on the Social Security Administration (SSA) Beneficiary Data Exchange file (BENDEX), which is received by DMS on a semi-monthly basis. A number of legitimate entitlements had erroneously been deleted (around 12,000). This accretion resulted in the expenditure of approximately \$5 million total funds for Buy-In premium payments.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CHS1-23: The Cabinet For Health Services Should Provide Better Safeguards For Funds Placed In Its Care (Continued)

Management's Response and Corrective Action Plan (Continued):

Background (Continued):

Additionally, approximately 4,800 new individuals were accreted as a result of a one-time issue that occurred during the processing of the Department's August recipient file.

Around early September DMS learned of issues related to the August file. As a result, DMS worked with CMS to resolve the issue and received permission from CMS to recreate the file. In the interest of time, DMS was advised by CMS to first take action to restore the deleted eligibles. Additionally, DMS was advised by CMS to then delete the accreted recipients after restoring the deleted recipients to full benefit status. Consequently, the new Input file due at the end of September 2004 had to be sent to CMS prior to DMS completion of the deletions in order to meet CMS timeframe for processing the file.

After processing the Input file, CMS submitted to DMS the Buy-In Billing file in early September, which included accretion files created by CMS. As a result of CMS processing the August Input file, Buy-In payments became due and were paid in the month of October totaling \$14,129,211.

DMS had anticipated a high level of activity on its August Buy-In file due to changes DMS made to its internal Buy-In file. In addition, CMS had made changes to Buy-In file layout and required states to follow new CMS procedures for the first time in August.

As soon as DMS learned of the issues with the file, DMS personnel immediately began working with CMS to take corrective action. DMS identified the discrepancy on the file during the second week of September 2004 and immediately contacted CMS to request permission to submit a modified Buy-In file to reverse the transactions, thereby averting an overpayment of funds. CMS policy does not provide for reversal of the transactions on the basis of the above-mentioned federal regulation, which states that once a file has been processed by CMS it will not be considered erroneous. 42 CFR 407.47(e).

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CHS1-23: The Cabinet For Health Services Should Provide Better Safeguards For Funds Placed In Its Care (Continued)

Management’s Response and Corrective Action Plan (Continued):

Background (Continued):

In September, DMS also requested reconsideration by CMS based on the payment amount in question. CMS did not reconsider and informed DMS that other states had made the same error. The example cited concerned New Jersey, which refused to make the premium payments as billed based on the erroneous data. As a result, the amount in question was deducted from New Jersey’s regular Medicaid federal funding. In addition, DMS recouped as many of the premium payments as allowed by federal law, which states that only three months of premium payment may be recouped.

Internal controls have been added to insure that any future changes to the Buy-In subsystem are approved at a director level. Currently, DMS continues its efforts to further refine the Buy-In process. DMS is also utilizing current consultants to evaluate further corrective action.

Agreement:

The Department for Medicaid Services agrees with the Auditor of Public Account’s (APA) recommendation that DMS should “review its payment procedures” and has taken active steps to insure accuracy in the Buy_in payment process.

Due to the specification of 42 CFR 407.47 (e), which states that “...If the state erroneously reports to SSA that an individual is a member of its coverage group, the rules of paragraphs (a) through (d) of this section apply, and coverage begins as though the individual were in fact a member of the group”, corrective action has been implemented which ensures that all Buy-In files are reviewed and analyzed by DMS and Medicaid’s fiscal agent (Unisys) staff prior to submission to CMS to identify and correct any inaccuracies.

Internal controls have been put in place through coding changes made to the Medicaid Management Information System (MMIS) to prevent a reoccurrence of this issue.

Currently, DMS personnel are manually reviewing the BENDEX data utilizing other data sources in order to prevent a reoccurrence of the situation.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CHS1-23: The Cabinet For Health Services Should Provide Better Safeguards For Funds Placed In Its Care (Continued)

Management's Response and Corrective Action Plan (Continued):

Agreement (Continued):

In addition, Medicaid is utilizing consultants to provide advice to the Department regarding implementation of additional internal controls including utilizing multiple files, or data sources, to verify the information DMS sends to CMS.

As a consequence of the August Buy-In events, the Kentucky Department of Justice and the Kentucky Office of the Inspector General are investigating DMS for the payments made to the recipients accreted in the August file. This investigation is ongoing and any findings will be utilized to implement further improvements to the Buy-In subsystem.

The Department for Medicaid Services appreciates the connotation of the APA's statement regarding the difficulty DMS would have experienced if it had simply refused to pay the indicated amount of Buy-In. That option would have placed thousands of Kentucky citizens in danger of losing their health insurance coverage.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CHS2-24: The Cabinet For Health Services Should Improve Efforts In Monitoring Subrecipient Activity

State Agency: Cabinet for Health Services

Federal Program: CFDA 93.283 – Centers for Disease Control and Prevention Investigations and Technical Assistance

Federal Agency: U.S. Department of Health and Human Services

Pass-Through Agency: Not Applicable

Compliance Area: Subrecipient Monitoring

Amount of Questioned Costs: None

The Department for Public Health (DPH) is responsible for monitoring subrecipient's use of federal awards. DPH performs monitoring through periodic site visits. The site visits assist in providing reasonable assurance that subrecipients administer federal assistance programs in compliance with laws, regulations, and the provisions of contracts or grant agreements and ensure that performance goals are achieved. DPH also has the responsibility to take prompt corrective action on any monitored audit findings within a reasonable time frame.

For fiscal year 2004, in addition to requiring site visits for those receiving federal awards, the department was required to have audits performed for 11 subrecipients who received \$5,490,369 of \$10,061,885 sent to subrecipients.

For testing purposes, we chose six (6) facilities that reported findings as a result of a site visit. For these site visits that resulted in any findings, we requested the corrective action plans for those facilities. Corrective actions plans for those facilities had either not been developed and/or implemented, until the request by the APA was made. Thus, DPH is not following up with their responsibility to monitor subrecipients and their plans for corrective action. They acknowledged this shortcoming in an email to the APA in which DPH states they are beginning to correct this problem

The Department for Public Health cannot be assured that the expended federal awards were for their intended purpose and complied with the requirements of OMB Circular A-133 without having proper monitoring procedures in place. We were unable to determine if the Department for Public Health evaluated the impact of subrecipient activities on the federal program and took timely and appropriate corrective action on any findings.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CHS2-24: The Cabinet For Health Services Should Improve Efforts In Monitoring Subrecipient Activity (Continued)

The Department for Public Health has the following responsibilities under OMB Circular A-133, Subpart D:

- 1) Ensure that subrecipients take prompt corrective action on any monitored audit findings; and,
- 2) Evaluate the impact of subrecipient activities on the pass-through entity's ability to comply with applicable Federal regulations.

Recommendation:

We recommend that the Department of Public Health ensure that A) appropriate corrective actions are taken on any subrecipient monitoring findings, and B) the auditors are able to review program compliance in the future.

Management's Response and Corrective Action Plan

This comment specifically concerns the financial management portion of the local agency review, which is conducted by the Division of Administration and Financial Management.

Corrective action has been taken by the Division. Effective July 1, 2004, the Division will monitor each local agency this state fiscal year. The Division is currently on track to complete all of the reviews by June 20, 2005. A tracking process is in place to ensure the site reviews are on schedule. Once this state fiscal year is completed, the Division will return to reviewing each local agency once every two years.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CWD9-25: The Department For Employment Services Should Implement Controls To Ensure Proper Review of Timesheets To Prevent Coding Errors

State Agency: Cabinet for Workforce Development

Federal Program: CFDA 17.207 – Employment Service

CFDA 17.801 – Disabled Veterans’ Outreach Program (DVOP)

CFDA 17.804 – Local Veterans’ Employment Representative Program

Federal Agency: U.S. Department of Labor

Pass-Through Agency: Not Applicable

Compliance Area: Activities Allowed/Unallowed and Allowable Costs/Cost Principles

Amount of Questioned Costs: None

During the test of compliance for the Activities Allowed/Allowable Cost requirement, the auditor noted the following weaknesses with the 48 payroll expenditures tested:

- Three (3) instances where the timesheet was not totaled correctly. These errors were not corrected when the supervisors reviewed the timesheets.
- Two (2) instances where the timesheet leave data did not match the Leave Balance Summary Report (Report 164).
- Five (5) instances where time was not appropriately distributed to the proper program code, based on the Payroll Distribution Charges Report (Report 153).

The auditor also noted eight (8) instances in which the hours charged on timesheets did not agree to the hours charged on Report 153. For example, an employee worked 83.5 hours (with no overtime) and the Report 153 showed 82.5 hours worked. The system defaulted to the standard pay period of 82.5 and no over ride code was entered to correct the employees time worked. This did not affect the employee’s salary or expenditures charged to federal programs.

The auditor found that adequate controls were not in place to prevent errors from going undetected.

As a result of the above errors, time charged to a program may not be accurate, which could result in an overstatement/understatement of indirect payroll costs. Errors on timesheets can go undetected when an adequate review process is not in place. Errors on timesheets could result in miscoding that affects other compliance requirements of the program. Errors when key punching the timesheet information into the system can create inconsistencies between printouts and actual timesheets.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CWD9-25: The Department For Employment Services Should Implement Controls To Ensure Proper Review of Timesheets To Prevent Coding Errors (Continued)

Per OMB Circular A-87:

[c]harges to federal awards for salaries and wages, whether treated as direct or indirect costs, will be based on payrolls documented in accordance with generally accepted practice of the governmental unit and approved by a responsible official(s) of the governmental unit . . . Where employees are expected to work solely on a single Federal award or cost objective, charges for their salaries and wages will be supported by periodic certifications that the employees worked solely on that program for the period covered by the certification . . . Where employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports . . .

Recommendation

We recommend the agency implement controls to ensure the following:

- Personnel are aware of the proper program codes for their assigned tasks.
- Employees are appropriately trained to ensure accuracy with timesheet preparation and review.
- Timesheet reviews verify that timesheet data has been accurately recorded into UPPS.

Management's Response and Corrective Action Plan

Controls are in place to help prevent inaccuracies for timesheet coding; however, we recognize that additional attention in this area is needed. Currently there are three levels control, the employee is responsible for accurately reporting his or her time, the supervisor is responsible for the first level of review and the area timekeeper performs the final level of review when the information is entered and extracted into the payroll system. The Time & Labor edit, in Document Direct, is the 4th control point; it is used to make corrections to default codes after payroll is entered. The timekeeper function is decentralized to the local office and branch level. Recent turnover of staff and staff shortages have been a contributing factors in the deficiencies found.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CWD9-25: The Department For Employment Services Should Implement Controls To Ensure Proper Review of Timesheets To Prevent Coding Errors (Continued)

Management's Response and Corrective Action Plan (Continued)

According to the Cabinet Payroll Manager, it is the responsibility of management or timekeepers to make the payroll area aware of errors made on leave balance summaries for changes. Errors are corrected when identified. These corrections will not reflect on the 153. Payroll has now been centralized to the Cabinet level; however, timekeeping remains a decentralized function.

When employees are working flex schedules and are not using override codes, the UPPS system automatically defaults to standard pay period hours. This is a system flaw that would take programming to rectify. Cabinet staff is aware of this issue.

This Office feels sufficient controls are in place to prevent inaccurate time sheet reporting; however, these controls must be strengthened through increased attention and additional training. The Office has already acknowledged the need for refresher training on timesheet coding. This issue was addressed with managers in the last OET Manager Meeting. Additional training is scheduled for the next meeting.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CWD10-26: The Department For Employment Services Should Strengthen Controls Over The Review And Approval Process For Allowable Costs

State Agency: Cabinet for Workforce Development

Federal Program: CFDA 17.207 – Employment Service

CFDA 17.801 – Disabled Veterans’ Outreach Program (DVOP)

CFDA 17.804 – Local Veterans’ Employment Representative Program

Federal Agency: U.S. Department of Labor

Pass-Through Agency: Not Applicable

Compliance Area: Activities Allowed/Unallowed and Allowable Costs/Cost Principles

Amount of Questioned Costs: None

While testing compliance with the allowable costs requirement for the Employment Services program, the auditor selected a transaction in the sample that was from a closed fraud case. The auditor requested the supporting information and found that the transaction was for the purchase of personal items at a retail grocery. The purchase was made on a retail grocery credit card that was issued in the agency’s name and had been requested by the agency to be destroyed. For the agencies’ purposes, the Kentucky State Police investigated this matter and referred it to the Franklin County Commonwealth Attorney for prosecution action. The former employee was ordered to pay \$6,688 in restitution. However for compliance purposes, the employee was charging the personal expenses to a cost allocation expenditure code that would then get allocated to different federal programs. Through discussion with the newly appointed Commissioner, it was noted in February 2005 that the DOL had never been notified of this situation. The agency informed the auditor that appropriate action was taken in the form of investigative work on behalf of the agency; however, there was no documentation provided to the auditor of the investigation or its results.

Through further inquiry, the auditor found that the supervisor of this employee was not adequately reviewing and properly approving documents; which allowed this situation to grow into thousands of dollars being mishandled. The supervisor approved several transactions that were in the auditor’s sample. Through conversations with the agency, it was noted the supervisor did not possess the knowledge or skills to approve program allowable cost transactions. This was supported as the expenditures were for personal items and not allowable costs under the program. The auditor is expanding the review to include other fiscal years’ expenditures for additional personal items that may have been approved.

During the same test addressed above, the auditor noted (2) two transactions that were for payment to CFC for monthly operational costs that are under an interagency lease agreement but no support was available. Upon discussion with agency personnel, the auditor was informed that detailed support was not normally provided to the agency.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CWD10-26: The Department For Employment Services Should Strengthen Controls Over The Review And Approval Process For Allowable Costs (Continued)

The auditor did obtain a copy of the interagency lease agreement but detailed invoices are not supplied to the agency to ensure that they are only billed for their portion of the operational costs.

Weak supervisory controls have led to a misuse of federal funds in the Employment Services program. The lack of adequate supervisory oversight allowed personal expenditures to be paid with program funds. When a supervising individual has limited knowledge of the system and allowable costs of the program, an employee can misuse program funds.

Inadequate supporting documentation can lead to overpayments being charged to the program.

Proper internal controls dictate that knowledgeable individuals provide adequate review and proper approval for transactions within the agency. There should be appropriate supervisory review by someone that has been trained and is aware of program allowable costs.

OMB Circular A-87 states,

2. Policy guides.

a. The application of these principles is based on the fundamental premises that:

- (1) Governmental units are responsible for the efficient and effective administration of Federal awards through the application of sound management practices.

Recommendation

We recommend CWD reevaluate the controls over transaction approval. We recommend that the agency ensure all supervisors are well trained and knowledgeable of the program's allowable costs when approving transactions. Also, upper level management should have appropriate oversight to ensure personnel are performing their job duties as outlined and documented in their performance evaluation.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CWD10-26: The Department For Employment Services Should Strengthen Controls Over The Review And Approval Process For Allowable Costs (Continued)

Recommendation (Continued)

We further recommend that CWD obtain and maintain all supporting documentation for program charges. This support should be obtained and reviewed prior to transaction approval and payment.

Finally, we also recommend FAC do a thorough review into the Commonwealth's credit card usage. During the course of this audit we confirmed credit cards (home improvement, retail stores, other credit card companies, etc.) other than ProCard were in existence in other state agencies. Unlike the extensive oversight procedures adopted by ProCard, no comprehensive inventory of these cards exists and the oversight procedures are unknown at the central level. We recommend FAC identify all non ProCard credit cards and either apply the appropriate FAP or cancel the cards.

Management's Response and Corrective Action Plan

CWD Response:

The Office of Employment and Training agrees with this finding. The credit card abuse was discovered by the Agency in December of 2003. An extensive review was completed upon discovery. P1 documents paid by the former employee in the quarter prior to discovery were 100% reviewed for potential abuse. Procurement cards, payments and expenditures were reviewed as well as Trade and KTAP payments for potential abuse. The Finance and Administration Cabinet ran a special report that provided a listing of all agency-mailed checks so these could be reviewed for fraud. Specific vendors, social security numbers, and ZZAdvantage documents were also queried and reviewed. Internal Security was involved and took the lead on the investigation. Staff in the Administration & Financial Management Division assisted Internal Security. The misuse of the credit card was the only fraudulent activity found. An Internal Security Report and additional documentation on the internal review is available. The Internal Security officer canceled the credit card in question after the abuse was found.

The employee in question is no longer with this agency. The supervisor that approved these payments has since been taken out of a supervisory role. The supervisor had been provided MARS training and had been advised on allowable

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FINDING 04-CWD10-26: The Department For Employment Services Should Strengthen Controls Over The Review And Approval Process For Allowable Costs (Continued)

Management's Response and Corrective Action Plan (Continued)

program expenditures. Performance Evaluations reflect the deficiencies of this supervisor. An additional level of review was put in place immediately after discovery of this problem. Since then, the responsibility for payment processing has moved to the Cabinet level.

Restitution has been made and deposited back into the Federal Programs that were originally charged.

II. The Cabinet for Health and Family Services (CHFS) creates an IX document for rental/property costs. We have consistently performed a responsibility test before approving IX documents but have not had the supporting detail to do more. CHFS has recently begun providing additional object code detail within the IX document. IX documents are created by CHFS from a MARS report. CHFS has agreed to begin providing OET a copy of the report to support all future IX documents.

FAC Response:

We agree with your recommendation and will be reviewing credit card usage by all state agencies. When the review is complete we will amend our Policy and Procedure Manual to limit use of credit cards to those specifically approved by the Finance and Administration Cabinet and in addition provide oversight similar to ProCard.

Auditor's Reply

During the course of the audit, the auditor spoke with agency personnel and the supporting documentation related to their work performed was not available. The auditor specifically asked for the information that was reviewed and all information, including what was pulled from the employee's desk was unavailable. Some information was attainable via internal security but nothing showing specific transactions reviewed by the agency. The auditor also spoke with the state police detective that investigated this situation and was once again

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CWD10-26: The Department For Employment Services Should Strengthen Controls Over The Review And Approval Process For Allowable Costs (Continued)

Auditor's Reply (Continued)

informed that the agency did not provide documentation of their review. Therefore, the auditor at this date has not witnessed any evidence of the agency's review.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CWD11-27: The Department For Employment Services Should Strengthen Controls To Ensure Compliance With Federal Earmarking Requirements

State Agency: Cabinet for Workforce Development

Federal Program: CFDA 17.207 – Employment Service

CFDA 17.801 – Disabled Veterans’ Outreach Program (DVOP)

CFDA 17.804 – Local Veterans’ Employment Representative Program

Federal Agency: U.S. Department of Labor

Pass-Through Agency: Not Applicable

Compliance Area: Earmarking and Reporting

Amount of Questioned Costs: None

During the test of compliance with the earmarking requirement, the auditor noted that the agency was not properly meeting and reporting accurately the percentages required under the Wagner-Peyser Act. Further investigation identified the agency consistently fell below the 10% earmarking requirement established by the Wagner-Peyser Act, but was reported as being met on the FSR 269 Report for grant number 2070200Z. Even though the report appeared accurate, the agency was performing journal vouchers to transfer expenditures to meet the earmarking requirement.

The agency was unable to provide supporting documentation to the auditor for the full amount that made up the 10% earmarking on their federal reports. They were taking expenditures that were not coded as an earmarking transaction and transferring them to an accounting code to meet the total dollar amount required. For example in the report above, the agency needed to have \$994,988 in expenditures for tasks outlined in the Wagner-Peyser Act to ensure that they met the earmarking requirement. They actually had \$604,762 in expenditures that were coded to the proper tasks outlined in the act and \$390,226 in expenditures that were transferred. These transfers enabled the agency to comply with the 10% requirement; however, there is no support to ensure the transfers were for specified tasks that would allow them to be coded to meet the earmarking requirement.

The justification that was provided to us to support the transfer was that the local offices were doing the work to meet the 10% as specified in the act, they were just not properly coding their time to reflect the tasks completed.

Inaccurate reports are being sent to the DOL when amounts are not supported by the services provided.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CWD11-27: The Department For Employment Services Should Strengthen Controls To Ensure Compliance With Federal Earmarking Requirements (Continued)

The Wagner- Peyser Act states:

SEC. 7. (a) Ninety percent of the sums allotted to each State pursuant to section 6 may be used--

(1) for job search and placement services to job seekers including counseling, testing, occupational and labor market information, assessment, and referral to employers;

(2) for appropriate recruitment services and special technical services for employers; and

(3) for any of the following activities:

(A) evaluation of programs;

(B) developing linkages between services funded under this Act and related Federal or State legislation, including the provision of labor exchange services at educational sites;

(C) providing services for workers who have received notice of permanent layoff or impending layoff, or workers in occupations which are experiencing limited demand due to technological change, impact of imports, or plant closures;

(D) developing and providing labor market and occupational information;

(E) developing a management information system and compiling and analyzing reports therefrom; and

(F) administering the work test for the State unemployment compensation system and providing job finding and placement services for unemployment insurance claimants.

(b) Ten percent of the sums allotted to each State pursuant to section 6 shall be reserved for use in accordance with this subsection by the Governor of each such State to provide--

(1) performance incentives for public employment service offices and programs, consistent with performance standards established by the Secretary, taking into account direct or indirect placements (including those resulting from self-directed job search or group job search activities assisted by such offices or programs), wages on entered employment, retention, and other appropriate factors;

(2) services for groups with special needs, carried out pursuant to joint agreements between the employment service and the appropriate ~~[private industry council]~~ **local workforce investment board** and chief elected official or officials or other public agencies or private nonprofit organizations; and

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FINDING 04-CWD11-27: The Department For Employment Services Should Strengthen Controls To Ensure Compliance With Federal Earmarking Requirements (Continued)

(3) the extra costs of exemplary models for delivering services of the types described in subsection (a).

Recommendation

We recommend the agency take corrective action to ensure that information submitted to the federal government is accurate and supported with proper documentation.

We recommend the agency ensure all employees understand the program requirements and report their time worked accordingly. The agency could provide additional training to employees so that services provided are coded correctly to support the proper time reporting of the earmarking compliance requirement.

Management's Response and Corrective Action Plan

The agency acknowledges that time coding that would capture the costs of activities within the realm of the earmarking requirement of the Wagner-Peyser (W/P) Act has been deficient. The adjusting entries done to reflect an amount of expenditure that satisfies the 10% requirement were done with the knowledge that significant amounts of qualifying activity was not directly charged to the code established for this purpose. The agency has documents on file that shows that 12 out of 28 field Branch Offices coded no time to the W/P 10% code and another five recorded less than 100 hours in the year. All offices engage in employer and client activity consistent with the earmarking requirement but time coding deficiencies have resulted in poor documentation of the eligible activities.

Corrective action has been initiated by way of notification to Branch Office managers providing a description of the services they provide that are eligible W/P 10% activity and a reminder of the coding used to record the activity. Individual follow-up is planned with those offices that recorded little or no 10% activity. A substantial turnover in managers has occurred in the last several years. The loss of experienced managers created the need for a training effort to make certain that the new group of managers possess the knowledge necessary for proper administration of programs and related matters such as time coding. This need was recognized even prior to this issue arising during the audit process. The agency discussed time coding with managers at a recent statewide meeting.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-CWD11-27: The Department For Employment Services Should Strengthen Controls To Ensure Compliance With Federal Earmarking Requirements (Continued)

Management's Response and Corrective Action Plan (Continued)

It was announced at the meeting that a workshop on service descriptions and time coding principles was being developed and was to be a main topic of the next statewide managers meeting planned to convene prior to the end of the current fiscal year.

It is recognized that an agency such as OET that is virtually 100% Federal funded through numerous individual program awards must maintain a very sound system of time recording by activity. This demand requires periodic refresher efforts for staff and management at the very least, and more intensive training following periods where large turnovers of management staff have occurred. OET management realizes the need for such ongoing administrative training and is making a strong commitment to this effort both to improve management and budget operations of the agency and as a corrective action plan to this audit finding.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-CWD12-28: The Department For Training And ReEmployment
Should Process Journal Vouchers Timely**

State Agency: Cabinet for Workforce Development

Federal Program: CFDA 17.258 – WIA Adult Grants

CFDA 17.259 – WIA Youth Grants

CFDA 17.260 – WIA Dislocated Workers

Federal Agency: U.S. Department of Labor

Pass-Through Agency: Not Applicable

Compliance Area: Reporting

Amount of Questioned Costs: None

During our review of internal controls over Reporting for the Workforce Investment Act, administered by the Department of Training and ReEmployment (DTR), we noted two problems.

First, for the National Emergency Grant (NEG) final federal report, line g, Federal unliquidated obligations, reported zero. However, a note on the supporting documentation indicated \$21,668 in “accrued expenses not posted @ Sept 2004.” Per a DTR employee, these expenses have not been posted as of February 23, 2005; however, they were incurred prior to June 30, 2004. A journal voucher will be done transferring allowable costs paid out of the 17.245-Trade Adjustment Assistance Workers grant to the NEG. The final report showing zero unliquidated obligations was submitted, when an unliquidated obligation amount of \$21,668 was indicated on the supporting documentation.

Second, the “cumulative expenditures to date” in the supporting documentation (Local Workforce Investment Area Roll-up worksheet) for the April to June 2004 quarterly financial report did not agree to the state’s accounting system (MARS) as follows:

For grants 27102 and 27302:

Report Area	Roll-up	MARS	Difference
Rapid Response (0730)	1,507,818	1,368,182	139,636
Adult Program (0750)	8,439,955	8,424,469	15,486

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-CWD12-28: The Department For Training And ReEmployment
Should Process Journal Vouchers Timely (Continued)**

For grants 27002, 27202, and 27402:

Report Area	Roll-up	MARS	Difference
Total Statewide (0720)	1,770,109	1,744,196	25,912
Rapid Response (0730)	23,331	23,185	145
Rapid Response Additional Assistance (0735)	519,849	508,186	11,663
Adult Program (0750)	2,720,980	2,828,277	-107,297
Dislocated Worker (0800)	1,479,360	1,372,063	107,297

All WIA funds are initially coded to 6500-0050 (unclassified reporting category) when drawn down into MARS. A journal voucher (JV) is done each quarter to transfer funds from 6500-0050 to the appropriate reporting category. The JVs were not done to distribute the drawdowns to the appropriate reporting category for the fourth quarter of 2004.

The FSR report submitted to the Federal government is not accurate. DTR had 90 days after the close of the NEG to record actual NEG expenditures on the accounting system. There is no documentation that the “accrued expenditures” relate to the NEG or were incurred prior to June 30, 2004.

The reporting categories in MARS do not agree to the roll-up expenditure report prepared by the agency for the fourth quarter of 2004. The employee responsible for preparing the JVs left the agency. The employee who assumed the responsibility for preparing the federal reports, did not prepare the JVs.

The instructions for completing line g of the FSR state, "Federal unliquidated obligations incurred by the project award recipient, for which an outlay (accrued expenditure) has not yet been recorded in the project award recipient's official accounting records. . . . On the final FSR, this line item should be zero. (Recipient has 90 days after all funds have been expended or the period of availability has expired to liquidate the accruals recorded during the period of performance.)."

Good internal controls dictate the accounting system properly reflects the expenditures for the WIA grants and that the federal reports agree or be reconciled to the accounting system.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-CWD12-28: The Department For Training And ReEmployment
Should Process Journal Vouchers Timely (Continued)**

Recommendation

We recommend DTR:

- contact the Federal government and inquire if a new final report needs to be submitted.
- prepare and process the appropriate journal vouchers as soon as possible.

Management's Response and Corrective Action Plan

OET agrees that the \$21,668.07 reported as "Accrued Expenditures" was not properly posted in MARS before the closeout period for the grant expired. To correct this situation, OET will revise the September 2004 "Final" Quarterly Report filed with Department of Labor (DOL) for the grant to remove the accrued expenditure amount and show the funds as being an "Unobligated Balance of Federal Funds."

OET agrees that the JVs to reclassify the LWIA drawdowns between reporting categories in MARS was not completed for the quarter ended June 2004. The auditor's statement that, "The reporting categories in MARS do not agree to the roll-up expenditure report prepared by the agency for the fourth quarter of 2004." is accurate, however, it is OET's contention that it is not necessary that the amounts match by reporting categories as long as the roll-up reports can be reconciled in total by grant to the amounts posted in MARS.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-CWD12-28: The Department For Training And ReEmployment
Should Process Journal Vouchers Timely (Continued)**

Management’s Response and Corrective Action Plan (Continued)

In the current process, all drawdowns requested by the LWIAs are posted by individual grant in MARS as 6500-0050 (Unclassified). OET would then use the expenses per cost category from the “roll-up expenditure reports” as the basis for the adjustment to reclassify the total expenses recorded in 6500-0050 Unclassified to various cost categories such as Youth (6500-0850), Adult (6500-0750) and Dislocated Worker (6500-0800) within those grants. Since OET uses the “roll-up expenditure report” as supporting documentation for expenses reported by cost category on the DOL Quarterly Reports and not the amounts reported in MARS by cost category, we found completing the JVs to reclassify the expenses within each grant by cost category to be a time-consuming and unnecessary process compared to the benefit received (none). OET does agree that the drawdowns posted to 6500-0050 by grant in MARS should be reconciled on a quarterly basis to the expenditures reported on the “roll-up expenditure report” and must agree in total at the time the grant is closed-out.

Auditor’s Reply

The expenditures by reporting category in MARS are incorrect. Good internal controls dictate that MARS should agree to the agency’s records. If the MARS accounting structure is not appropriately tracking expenditures, the agency should review the accounting structure for the WIA programs and make changes accordingly. Until the accounting system is changed, a JV should be done to ensure MARS and the agency’s records agree. Other agencies or personnel within CWD may use the MARS information.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DFWR1-29: The Department Of Fish And Wildlife Resources Should Ensure That All Timesheets Are Signed By The Employee And The Supervisor

State Agency: Department of Fish & Wildlife Resources
Federal Program: CFDA 15.605—Sport Fish Restoration
CFDA 15.611—Wildlife Restoration
Federal Agency: U.S. Department of the Interior
Pass-Through Agency: Not Applicable
Compliance: Activities Allowed and Allowable Costs
Amounts of Questioned Costs: None

During testing of payroll for activities allowed there were three instances where supervisors timesheets were not signed by the next line supervisor or director.

Timesheets not signed by the next line supervisor or director may be incorrectly coded to the wrong grant, program budget unit, fund, and project. Failure to have timesheets approved at all levels may lead to employees miscoding time.

Payroll Manual: Chapter 5 – Reporting Time and Attendance of Employees states:
“Keeping records of time and attendance for each employee is required both to satisfy good auditing controls and to comply with requirements of the Federal Government under the provisions of the Fair Labor Standards Acts. A part of these requirements dictate that time records are kept on a daily basis. In addition, the time records must have both the employee’s and the employee’s supervisor’s original signatures certifying to the accuracy of the time reported.

No state agency is required to use the statewide time and attendance form. A substitute developed by the agency must be used. However, any substitution must provide for daily reporting, employee signature and supervisor signature.”

Recommendation

We recommend that all timesheets signed by both the employee and supervisor to ensure that time is being coded to the correct grant, program budget unit, fund, and project.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DFWR1-29: The Department Of Fish And Wildlife Resources Should Ensure That All Timesheets Are Signed By The Employee And The Supervisor (Continued)

Management's Response and Corrective Action Plan

We agree that both the employee and the direct supervisor must sign the timesheet. We are conducting training sessions on timesheet procedures. The focus of the training sessions is to ensure that each employee is aware that he/she is responsible for reporting accurately and on time his/her hours worked, the cost centers and grants or projects to which the hours should be charged, and any authorized absences. We are stressing that both the employee and supervisor must sign the timesheet, and that their signatures indicate the information contained on the timesheet is correct, and the timesheet has been accurately and thoroughly completed.

We will review timesheets for accuracy and compliance on a scheduled basis once we have hired the Graduate Accountant Manager and Internal Policy Analyst (Grant Accountant).

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DFWR2-30: The Department Of Fish And Wildlife Resources Should Consider Requesting The General Assembly To Adopt 50 CFR 80.3-80.4 Into State Law

State Agency: Department of Fish & Wildlife Resources
Federal Program: CFDA 15.605—Sport Fish Restoration
CFDA 15.611—Wildlife Restoration
Federal Agency: U.S. Department of the Interior
Pass-Through Agency: Not Applicable
Compliance: Special Tests and Provisions
Amounts of Questioned Costs: None

As required by Code of Federal Regulations, 50 CFR80 section 3 and 4 there is a statutory prohibition to prevent diversion of license revenue. However, during review of the internal control questionnaire, section N “Special Tests and Provisions,” we became aware that the General Assembly can transfer funds from the Game and Fish Fund to the general fund as needed. This is prohibited by federal regulations. During fiscal year 2004 the Department of Fish and Wildlife did not transfer out any funds from the Fish and Game Fund to the General Fund. For FYE 6/30/2004, Fish and Wildlife generated \$21,062,348 in license revenue.

The General Assembly has the authority, in appropriating funds, to transfer funding by “notwithstanding” certain statutes. In the case of the Department of Fish and Wildlife Resources, Federal funds could be jeopardized by such action.

KRS 150.150 Game and Fish fund states (1):

- (1) “Except as provided in this chapter, all moneys derived from the sale of licenses or from any other source connected with the administration of this chapter shall be promptly paid over to the State Treasurer, who shall deposit such moneys in a special fund, known as the game and fish fund. The game and fish fund shall be used to carry out the purposes of this chapter and any law or regulation for the protection of wildlife and for no other purpose.”

KRS 48.315 Transfer of agency, special, and other funds to general fund in budget bill states,

- (1) “The General Assembly may provide in a budget bill for the transfer to the general fund all or part of the agency funds, special funds, or other funds established under the provisions of ...KRS 150.150...”

**COMMONWEALTH OF KENTUCKY
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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DFWR2-30: The Department Of Fish And Wildlife Resources Should Consider Requesting The General Assembly To Adopt 50 CFR 80.3-80.4 Into State Law (Continued)

Recommendation

The Department of Fish and Wildlife Resources should consider requesting the General Assembly to adopt the provisions of 50 CFR 80.3-80.4 into state law to further assure no loss of Federal funds due to the transfer from a restricted agency account.

Management's Response and Corrective Action Plan

We agree with your recommendation. Fish and Wildlife Resources is aware that the Federal Regulations 50 CFR 80.3-80.4 states that the Commonwealth should enact a state law to assure that funds from license revenue are not transferred from the agency into the general fund or else where. House Bill 457 included the Assent language as required by the Federal Regulations. However, both houses of the General Assembly did not pass the bill. As a result, we continue to be in non-compliance with CFR 80.3-80.4.

We will try again during the next session.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DFWR3-31: The Department Of Fish And Wildlife Resources Should Implement Procedures To Ensure Program Income Is Properly Accounted For And Recorded In The System

State Agency: Department of Fish & Wildlife Resources

Federal Program: CFDA 15.605—Sport Fish Restoration
CFDA 15.611—Wildlife Restoration

Federal Agency: U.S. Department of the Interior

Pass-Through Agency: Not Applicable

Compliance: Program Income

Amounts of Questioned Costs: None

The Department of Fish and Wildlife Resources receives program income from land purchased, improved, or maintained with Federal funds. In FY 04 the Department of Fish and Wildlife received \$677,830 in program income. During our test of program income there was one out of ten instances where the amount per the cash receipt (CR) document did not agree to the supporting documentation.

Due to staff shortages, the same person receives the income, deposits the money with Treasury and then performs the reconciliations. There is no final review to ensure all income received is deposited. Without proper internal controls the risk increases for unrecorded or miscoded program income.

Internal control over the handling of cash and checks is one of the most critical areas in the receipt process. Proper segregation of duties relating to cash demands that close consideration be given to these various activities. Separation of cash handling and record keeping should exist.

Recommendation

We recommend that procedures be implemented to ensure that program income is properly accounted for and recorded in the system. There should be a separate person in charge of depositing the funds and performing the reconciliation. Supervisory review is necessary as well.

Management's Response and Corrective Action Plan

We agree with your recommendation. Fish and Wildlife Resources is aware that Administrative Services has internal control weaknesses. We are cognizant that there should be proper segregation of duties. Also, we recognize that the handling of cash and checks is one of the most critical areas in the receipt

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DFWR3-31: The Department Of Fish And Wildlife Resources Should Implement Procedures To Ensure Program Income Is Properly Accounted For And Recorded In The System (Continued)

Management's Response and Corrective Action Plan (Continued)

process. However, we have been forced to direct employees to perform duties that should be separated in order to get the job done. This action was taken because we are under staffed.

We will implement your recommendation as soon as we fill our current vacancies.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA1-32: The Department Of Military Affairs Should Develop Internal Control Procedures To Retain The Documentation Used To Compute The Payroll Cost Allocation Plan

State Agency: Department of Military Affairs

Federal Program: CFDA 12.401 – National Guard Military Operations And Maintenance (O&M) Projects

Federal Agency: U.S. Department of Defense

Pass-Through Agency: Not Applicable

Compliance Area: Allowable Costs / Cost Principles

Amount of Questioned Costs: None

The Department of Military Affairs has developed and uses a Cost Allocation Plan to distribute payroll charges for employees who can have all or part of their salary charged to federal programs. Participation rates originate in three ways. One component (titled VAS2) involves employees chargeable directly to one of the Cooperative Agreements between the state and federal government. Another component (titled FAC2 – primarily Frankfort employees who work on various Cooperative Agreements) involves computing the documents examined for each area and charging the percentage worked in each area as the participation rate. The final component (titled GMM2) involves employees who work at the various armories throughout the state in support of federal activities.

We randomly selected 45 employees to examine the underlying documentation supporting the various participation rates and noted the following (relating to FAC2):

- Six instances where the participation rates were agreed to an agency prepared summary sheet. However, neither the underlying computerized files nor the paper copies had been retained so that we could verify how these percentages were computed.
- Fifteen instances where Military Affairs did not provide documentation for the participation rates charged.
- Three instances where the participation rates were agreed to an agency prepared summary sheet, however, at least one of the participation rate percentages were not listed on this summary page. Again, as noted above, neither the underlying computerized files nor the paper copies had been retained so that we could verify how these percentages were computed.

Also, Military Affairs did not have detailed written procedures to explain how the FAC2 participation rates were compiled.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA1-32: The Department Of Military Affairs Should Develop Internal Control Procedures To Retain The Documentation Used To Compute The Payroll Cost Allocation Plan (Continued)

The employee who prepared the FAC2 cost allocation plan for state fiscal years 03 & 04 left the agency. The computerized files used to compute the participation rates were not retained and evidently a hard copy was not prepared for all the files.

OMB Circular A-87 Attachment A, Part C, j. requires expenditures to be adequately documented.

Agencies should prepare detailed written procedure for all vital processes within an agency. These written procedures would allow replacement employees or management to continue performing crucial processes in a consistent and functional manner.

Recommendation

We recommend Military Affairs implement the following:

- Develop a policy to retain detailed supporting documentation to support all costs charged to federal programs.
- Develop detailed written procedures of the payroll cost allocation plan.

Management Response and Corrective Action Plan

Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for allowable cost / cost principles is to provide reasonable assurance that Federal grant awards are expended only for allowable activities and that the costs of goods and services charged to Federal grant awards are allowable and in accordance with the applicable cost principles. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.

Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department that identified the fact that resource constraints have increased the overall risk to compliance standard accomplishment. From SFY2002 to SFY2004, DMA's federal grant

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FINDING 04-DMA1-32: The Department Of Military Affairs Should Develop Internal Control Procedures To Retain The Documentation Used To Compute The Payroll Cost Allocation Plan (Continued)

Management Response and Corrective Action Plan (Continued)

awards disbursement amount increased by 190% yet at the same time DMA lost 11% of its full time state employee workforce in the last budget reduction cycle due to inability to fully fund available positions from appropriated state General Funds. While DMA management, at all levels, has taken steps to mitigate the increased risk, the fundamental issue remains that doing more with less can adversely effect the risk of noncompliance to internal control standards. Managing this increased risk, without addressing the systemic problem directly, is a very difficult management challenge.

DMA concurs with the auditor's finding and has developed a corrective action plan designed to restore compliance and insure future compliance.

The Division of Facilities Management's Cost Allocation Administrator has detailed a corrective action task list and has already initiated action to correct the findings as described below:

- 1. Effective with the Federal Budget for FY05, the Facilities Division has established a uniform method to calculate the allocation percentages for Skilled Trades, Property Management, Administrative Services, Administrative Supervisors and Managers, and Reimbursement Administrative Services and to retain source documentation of these direct Cost Allocation calculations.*
- 2. No later than July 31st annually, the Facilities Division Cost Allocation administrator shall review the job duties of all Facilities employees with the Administrative Branch Manager or Assistant Director to assign each employee to a funding source (100% federal, direct cost allocation, or 100% state) based on documented evidence of prior state fiscal year work performed directly for a federal grant program. Employees whose work is exclusively for a federal grant program shall be categorized as 100% federally reimbursable IAW the federal grant guidelines. Employees who do not perform work, fully or partially, for any federal grant program shall be categorized as 100% state funded. Employees who perform some work or*

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA1-32: The Department Of Military Affairs Should Develop Internal Control Procedures To Retain The Documentation Used To Compute The Payroll Cost Allocation Plan (Continued)

Management Response and Corrective Action Plan (Continued)

services directly for a federal grant program shall be tabulated via a direct cost allocation process. These employees, whose pay and expenses qualify for direct cost allocation, are further subdivided by functional section:

- *Skilled Trades: all those employees who's work involves repair and maintenance of facilities;*
 - *Property Management: all those employees who's work involves supplying all facilities with required equipment and supplies to maintain operations;*
 - *Administrative Services: all those employees who's work involves central services activities;*
 - *Administrative Supervisors and Managers: all those employees who supervise the central service activities;*
 - *Reimbursement Section: all those employees who's work involves the reimbursement of state funds by federal funds – these employees are 100% federally funded and allocated to all federal grant projects.*
3. *For each sub-category of direct Cost Allocation personnel, the appropriate reports shall be gathered to document the proportional direct cost benefit using the same state fiscal year time period for all historical reports:*
- *Skilled Tradesmen: Historical work order transaction data shall be used to support allocated direct labor costs. Each work order entered into the system is assigned a Fund ID. These 'Fund ID's represent the program responsible for the cost of repairs.*
 - *Property Management: These employees do not use any definitive documentation that tracks their activities by program or facility. Therefore, the best allocation method shall use the square footage of reimbursed facilities divided by total square footage of all facilities. The Federal government provides both the square footage of each facility and the Agreement code for each facility. Training centers, code TSC, and UTES/MATES/AASF buildings, code SC8, are all funded through AYOM training. Logistical facilities, code SCS, are funded through AYOM log.*

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA1-32: The Department Of Military Affairs Should Develop Internal Control Procedures To Retain The Documentation Used To Compute The Payroll Cost Allocation Plan (Continued)

Management Response and Corrective Action Plan (Continued)

- *Administrative Services Section: Historical MRDB transaction data shall be used to support allocated central service costs. These reports count the number of transaction line entries made to the specialized ledgers. These reports shall exclude any document categories not applicable to facilities. For example, all documents prepared or processed by Emergency Management are excluded because the facilities division does not work on or use Emergency Management projects and documents. These reports include the percent of transaction lines made for a given project / CFDA program / CFDA agency as compared to all transactions made within the reporting period.*
 - *Administrative Supervisors and Managers: This group uses the same reports as Administrative Services Section explained above. The only difference is that upper management is not reimbursable through all programs. Both Supervisors and Managers are charged to the Army O&M project based upon the allocation percent. However, reimbursement is only allowable for the Supervisors under the Army Environmental grant program agreement.*
 - *Reimbursement Section: Historical MRDB transaction data is used to support allocated reimbursement personnel costs. The reports count the number of transaction line entries made to the specialized ledgers. The reports excluded any document categories not applicable to reimbursement. For example, USAR projects are included with the Administrative Services Section, but not on the Reimbursement reports. These reports include the percent of transaction lines made for a given project / CFDA program / CFDA agency as compared to all transactions made within the reporting period.*
4. *No later than July 31st annually, the Facilities Division Cost Allocation Administrator shall run and file all source data MRDB reports which shall be kept in the appropriate folder by the Facilities Division reimbursement section. The Facilities Division Cost Allocation Administrator shall prepare a direct cost allocation memo, based on the MRDB source data reports, and send it to the Facilities Division Director and the federal grantor (FMO) for*

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA1-32: The Department Of Military Affairs Should Develop Internal Control Procedures To Retain The Documentation Used To Compute The Payroll Cost Allocation Plan (Continued)

Management Response and Corrective Action Plan (Continued)

approval and implementation on October 1st annually. This memo will contain work sheets that provide the indirect cost allocation by individual employee as based on the source documentation reports.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA2-33: The Department Of Military Affairs Should Implement Internal Control Procedures To Comply With NGR 5-1/ANGI 63-101 Relating To Program Income For The National Guard Program

State Agency: Department of Military Affairs

Federal Program: CFDA 12.401 – National Guard Military Operations And Maintenance (O&M) Projects

Federal Agency: U.S. Department of Defense

Pass-Through Agency: Not Applicable

Compliance Area: Program Income

Amount of Questioned Costs: None

Federal statute NGR 5-1/ANGI 63-101 allows income from the rental of state-owned, federal supported armories to be used to maintain the armories. The Division of Facilities Management oversees and monitors the financial operation of each armory via review of the monthly (in some instances quarterly) Installation Management Fund Cash Account & Operating Statement. These reports should include bank statements, cancelled checks, rental agreements and detail supporting documentation for all expenditures. Based on information provided by the agency, the armories handled over \$220,000 in these accounts for FY 04.

We examined the monthly reports filed during FYE 6/30/04 for five of the armories and noted the following:

- Per Military Affairs personnel, some state employees have been compensated for serving as armory managers. This would appear to violate the state's Conflict of Interest Policy found in KRS 11A.040 (4) & (5) and U. S. Department of Labor overtime laws. KRS 11A.040 (4) and (5) state "A public servant shall not knowingly himself or through any business in which he owns or controls an interest of more than five percent (5%), or by any other person for his use or benefit or on his account, undertake, execute, hold, bid on, negotiate, or enjoy, in whole or in part, any contract, agreement, lease, sale, or purchase made, entered into, awarded, or granted by the agency by which he is employed or which he supervises, subject to the provisions of KRS 45A.340. (5) A public servant shall not knowingly accept compensation, other than that provided by law for public servants, for performance of his official duties without the prior approval of the commission." Also, 101 KAR 2:102 Section 5 (c) which incorporates U. S. Department of Labor regulations, states "An employee deemed to be "nonexempt" by the provisions of the FLSA shall be compensated for hours worked in excess of forty (40) per week as provided by subparagraphs 1 to 3 of this paragraph."

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA2-33: The Department Of Military Affairs Should Implement Internal Control Procedures To Comply With NGR 5-1/ANGI 63-101 Relating To Program Income For The National Guard Program (Continued)

- Four of the armories did not consistently submit rental agreements, or any other type of receipt summary, each month to support the amounts deposited. The lack of adequate supporting documentation and the lack of uniquely or prenumbered rental contracts precluded us from determining that all funds received had in fact been deposited. Also, Military Affairs personnel indicated that approximately 95% of the armories have snack and soft drink machines. We noted evidence of snack and soft drink machines for only two of the five armories reviewed. Military Affairs policy DMAR 210-8 Section VI c. states “The Standard Voucher (AGO Ky Form 27-2) when used as a receipt record will have supporting documents attached (rental, contracts, vending deposits, bank deposits, etc.). If supporting documentation is used in the previous report, reference only is required.”
- We could not find documented prior approval for a \$558.60 purchase of tables by the Richmond Armory. Military Affairs policy DMAR 210-8 Section III c. requires prior approval for any non-recurring purchase over \$50.
- The Richmond Armory purchased carpet for \$476.00 but did not provide any supporting documentation. Military Affairs policy DMAR 210-8 Section VI d. requires expenditures to have supporting documentation
- The Owensboro Armory reimbursed an employee twice for the use of their private vehicle. The employee was reimbursed at \$.50 per mile from the Installation Management Fund bank account. Per Military Affairs personnel, this is not an allowable use of armory funds. Reimbursements to employees (federal or state) for mileage should be submitted through the normal travel reimbursement process instead of being paid by the armory fund.
- Many of the armory managers would write checks to themselves for security or clean-up relating to a specific rental event. While this is allowable under current Military Affairs procedures, this process impedes separation of duties and lacks the appearance of an arms-length transaction. Good internal control procedures require that adequate documentation be submitted to allow for the verification of all deposits and expenditures. Also, these procedures would provide for adequate separation of duties and the evidence of an arms-length transaction.
- For four of the five armories tested, the bank statement amounts did not agree to the amounts recorded on the Installation Management Fund Year End Balances Report.

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FINDING 04-DMA2-33: The Department Of Military Affairs Should Implement Internal Control Procedures To Comply With NGR 5-1/ANGI 63-101 Relating To Program Income For The National Guard Program (Continued)

- The Danville Armory received a cold check for the rental of the armory; neither Military Affairs personnel nor we could determine if this had been collected and redeposited.
- We noted several individuals had received over \$600 for services provided (including the armory managers). However, these individuals were not provided with a 1099 Miscellaneous form indicating the amount of taxable wages. Internal Revenue regulations require that anyone providing services totaling over \$600 in a calendar year shall be issued a 1099 Miscellaneous form denoting the non-employee taxable earnings.

When notified of a change in armory managers, Military Affairs sends each manager a packet including sample monthly reports, policies and procedures, blank rental agreements, etc. However, Military Affairs personnel indicated, due to active duty requirements of the armory managers there is a large turnover in this position. Also, many times armories do not notify Military Affairs on a timely basis of changes in armory managers. These new managers lack familiarity with the required procedures thus creating errors and omissions.

Recommendation

We recommend Military Affairs implement the following:

- Military Affairs should consult with the Executive Branch Ethics Commission to determine if state employees performing certain duties at the armories may be compensated with additional salary as provided by current agency policy. In addition, Military Affairs should consult with the Personnel Cabinet to determine if other wage and applicable labor provisions are being met.
- Require rental agreements, a detail of receipts and/or AGO Form 27-2 to support all deposits for the month. Enough detail should be provided to allow the Military Affairs reviewer to agree documentation to the amount recorded by the bank.
- Develop a process to pre-number rental contracts for each armory and perform a monthly reconciliation to ensure all contracts are accounted for and submitted with the monthly report.
- Military Affairs inquire of all armories as to who has vending revenues and ensuring these funds are being reported on the monthly reports.
- Remind armories to obtain prior approval for purchases over \$50 and to supply supporting documentation for all expenditures.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA2-33: The Department Of Military Affairs Should Implement Internal Control Procedures To Comply With NGR 5-1/ANGI 63-101 Relating To Program Income For The National Guard Program (Continued)

Recommendation (Continued)

- Notify armory managers that reimbursements for mileage are not an allowable expenditure.
- Develop a policy requiring review and approval of all payments made to armory managers by their commanding officer or someone else with supervisory responsibilities.
- Ensure amounts recorded on the Installation Management Fund Year End Balance Report agree to bank statements.
- Develop a system, either at the armory or at Military Affairs, tracking amounts received by individuals and ensuring that the proper tax forms are prepared. Each person paid for providing services to the armory should complete a W-9 prior to any payment being made.

Management Response and Corrective Action Plan

Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for program income is to provide reasonable assurance that federal grant related program income is correctly earned, recorded, and used in accordance with the federal grant program requirements. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.

DMA concurs with the auditor's finding and has developed a corrective action plan designed to restore compliance and insure future compliance.

The Division of Facilities Management's IMF Fund Administrator has detailed a corrective action task list and has already initiated action to correct the findings as described below:

- 1. The Facilities Management Division has already submitted an analysis request to Mr. Jo Ledford, with the Executive Branch Ethics Commission, on the issue of the ten percent armory manager compensation wage. We will*

**COMMONWEALTH OF KENTUCKY
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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA2-33: The Department Of Military Affairs Should Implement Internal Control Procedures To Comply With NGR 5-1/ANGI 63-101 Relating To Program Income For The National Guard Program (Continued)

Management Response and Corrective Action Plan (Continued)

make the appropriate adjustments to the Installation Management Fund Rules & Regulations according to Mr. Ledford's ruling. The estimated completion date for this task is June 30, 2005.

- 2. Effective immediately, all armory managers and others who perform any armory rental security or clean-up shall be required to complete a W-9 form in order to track the annual income collected through armory rental clean-up, security and the ten percent armory manager compensation wage. Armory managers will be required to complete a separate AGO 27-2 form to show their monthly compensation wage and any hours of security & clean up they may have done during/after an armory rental. If the armory manager chose to allow another employee to perform the maintenance and security, he or she is to submit an AGO 27-2 form for that person, to include the hours worked during the armory rental. The Facilities Division IMFFund Administrator shall track this data on a monthly basis according to the amounts reported on each statement. This will allow the Facilities Division IMF Fund Administrator to track the annual income these employees have earned through these services and will ensure that the proper tax documents are provided. The estimated completion date for this task is December 31, 2005.*
- 3. Concerning the deposits made by armory managers, more detailed documentation shall be required by the Facilities Division IMF Fund Administrator to show the source of all deposited funds. Beginning 1 July 2005 armory managers will be required to provide a detailed breakdown of deposited funds on an AGO 27-2 form. The Facilities Division IMF Fund Administrator shall also require that all rental agreements be attached to the monthly statements for the month during which the rental took place. For more efficient tracking purposes, the Facilities Division IMF Fund Administrator shall order pre-numbered rental agreements for armory managers to begin using at the start of SFY 2006. This will ensure that all agreements are accounted for. The estimated completion date for this task is June 30, 2005.*

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA2-33: The Department Of Military Affairs Should Implement Internal Control Procedures To Comply With NGR 5-1/ANGI 63-101 Relating To Program Income For The National Guard Program (Continued)

Management Response and Corrective Action Plan (Continued)

4. *Beginning with the SFY2005 IMF Year End Balance Report, the Facilities Division IMF Fund Administrator shall ensure the IMF Year End Balance Report corresponds to the monthly bank statements. The estimated completion date of this task is June 30, 2005.*
5. *No later than March 31, 2005, Facilities Management Division shall make the appropriate changes to the Installation Management Fund Rules & Regulations to include all of the above-mentioned revisions.*
6. *No later than June 30, 2005, the Facilities Division IMF fund administrator shall meet with all armory managers to discuss the changes to the IMF Rules & Regulations. Items for discussion shall include the requirements of each monthly statement and what a complete statement should consist of, stress the importance of the rules & regulations, and answer and address any questions or concerns they may have.*
7. *No later than June 30, 2005, the Facilities Division IMF Fund Administrator shall verify which armories have vending machines and work with the DMA Procurement Officer to get all Armories on state contract for vending services and have all earnings checks sent through the Facilities Division IMF Fund Administrator for deposit in the appropriate Armory IMF fund.*

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA3-34: The Department Of Military Affairs Should Implement Internal Controls To Retain Supporting Documentation For PX Documents

State Agency: Department of Military Affairs

Federal Program: CFDA 97.036 – Public Assistance Grants

Federal Agency: U.S. Department of Homeland Security

Pass-Through Agency: Not Applicable

Compliance Area: Allowable Costs/Cost Principles

Amount of Questioned Costs: \$98,678.70

The MARS user guide for Projects and Grants allows the use of PX documents to record indirect transactions for a project or grant. These charges may include allocated administrative expenses; items purchased in bulk in prior fiscal years and used in the current fiscal year; payments for administrative expenses relating to disasters incurred in a previous fiscal year; or recording amounts incurred by subrecipient state agencies. The affected division will prepare the PX document and along with supporting documentation forward to the Division of Administrative Services for final MARS approval.

We tested 11 PX documents, six relating to the 97.036 - Public Assistance Grants Program and five relating to the 12.401 National Guard Program and noted the following:

- One document, totaling \$98,721.52, could not be located
- One document, totaling \$(42.82), did not have supporting documentation
- Two documents did not have the necessary documentation from the prior fiscal year to allow us to determine where and when the original charge had been made (no questioned costs).

All the errors noted above relate to the 97.036 - Public Assistance Program. The PX document was used 19 times, totaling \$681,327.77. As noted above, four documents were in error or 21% of the total documents and the unsupported expenditures (questioned costs) equaled 14.5% of the dollar amount charged. OMB Circular A-87 Attachment A, Part C, j. requires expenditures “be adequately documented.”

Agency policy requires PX documents be sent to Administrative Services Division with all applicable supporting documentation. This policy was not followed and resulted in our questioning the costs for the missing documentation. Also, Military Affairs has a policy requiring all PX documents be sent to the Administrative Services Division for final approval. This policy requires either the Division preparing the PX or Administrative Services make a copy of all the PX documents and the supporting documentation.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA3-34: The Department Of Military Affairs Should Implement Internal Controls To Retain Supporting Documentation For PX Documents (Continued)

Recommendation

We recommend Military Affairs reinforce and adhere to the policy of making copies of all PX documents and applicable supporting documentation.

Management Response and Corrective Action Plan

Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for allowable cost / cost principles is to provide reasonable assurance that Federal grant awards are expended only for allowable activities and that the costs of goods and services charged to Federal grant awards are allowable and in accordance with the applicable cost principles. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.

DMA concurs with the auditor's finding and has developed a corrective action plan designed to restore compliance and insure future compliance.

The Administrative Services Fiscal Manager has detailed a corrective action task list and shall initiate action to correct the findings as described below:

- Effective immediately, all Advantage disbursement and non-accounting PX documents will be prepared and processed by a DMA division utilizing Advantage level 1 & 2 approval and then forwarded to the Admin Services Fiscal Manager for final processing and level 3 agency approval. The Admin Services Fiscal Manager, exercising final agency approval, will insure that all documents have appropriate source documentation attached before final approval and that, upon final approval, primary and source documents are properly filed in the Agency's official financial files.*

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DVA1-35: The Kentucky Department of Veterans Affairs Should Design and Implement Internal Controls Over Compliance With Federal Program Requirements

State Agency: Department of Veterans Affairs

Federal Program: CFDA 64.203 – State Cemetery Grants

Federal Agency: U.S. Department of Veterans Affairs

Pass-Through Agency: Not Applicable

Compliance Area: Activities Allowed, Allowable Costs, Special Tests and Provisions

Amount of Questioned Costs: None

Based on inquiry and observation, the agency lacks internal controls over compliance with Federal program requirements. For example:

- The agency does not review its purchases for allowability as determined in OMB Circular A-87 or other SCG program-specific literature.
- The agency does not review construction costs, which are paid and recorded by Finance, for allowability as determined in OMB Circular A-87 or other SCG program-specific literature.

Although Finance does administer the construction part of the SCG program, which is the majority of expenditures, KDVA is responsible for ensuring compliance with Federal program requirements.

The lack of controls is due to turnover of personnel and a lack of experience in Federal grant management. The absence of internal controls increases the risk of noncompliance with federal program requirements.

According to OMB Circular A-133, Subpart C, Section .300(b), “the auditee shall maintain internal control over Federal programs that provides reasonable assurance that the auditee is managing Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs.”

Recommendation

We recommend that individuals involved in the SCG program review Part 6 of the Compliance Supplement to OMB Circular A-133. We recommend that the agency then implement their choice of internal controls suggested in the Compliance Supplement. All five components of internal control should be

**COMMONWEALTH OF KENTUCKY
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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DVA1-35: The Kentucky Department of Veterans Affairs Should Design and Implement Internal Controls Over Compliance With Federal Program Requirements (Continued)

Recommendation (Continued)

addressed for each applicable program requirement. The agency should ensure that adequate records are maintained to provide evidence of the existence of any internal controls that are implemented.

Management's Response and Corrective Action Plan

KDVA does not have purchase authority as far as it concerns the construction process of the cemetery. The finance cabinet controls the contract and all purchase and change orders that are involved in the construction phase of the SCG program. Although, during the construction phase of the SCG program, there is at a minimum a monthly progress meeting which KDVA has a representative attend each one of those meetings. We have attached a copy of each of these monthly meeting minutes to this memo (not included), which show that there is a representative of KDVA at each one of these meetings. These notes are also forwarded to the Commissioner of KDVA and the Branch Manager of the cemeteries, which is shown in the notes. KDVA keeps abreast of all construction issues and expenditures.

Auditor's Reply

KDVA does not need purchase authority for the construction process in order to be able to review supporting documentation of expenditures for allowability. State procurement policies and procedures do not supersede Federal program requirements.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DVA2-36: The Kentucky Department of Veterans Affairs Should Monitor Grant Supported Activities to Assure Compliance With Applicable Federal Requirements

State Agency: Department of Veterans Affairs

Federal Program: CFDA 64.203 – State Cemetery Grants

Federal Agency: U.S. Department of Veterans Affairs

Pass-Through Agency: Not Applicable

Compliance Area: Special Tests and Provisions

Amount of Questioned Costs: None

Based on inquiry, observation, and testing of inspections, the requirements of the Code of Federal Regulations (CFR) are not being met in the following manner; KDVA management does not adequately monitor grant expenditures and grant supported activities in order to assure compliance with Federal program requirements.

The noncompliance was caused by a lack of internal control over compliance and a lack of experience in Federal grant management. Noncompliance with federal program requirements could cause a loss of federal funding.

38 CFR 43.40(a) states that “grantees are responsible for managing the day-today operations of grant and subgrant supported activities. Grantees must monitor grant and subgrant supported activities to assure compliance with applicable Federal requirements and that performance goals are being achieved. Grantee monitoring must cover each program, function or activity”.

Recommendation

We recommend that personnel involved in the SCG program review the requirements of the Code of Federal Regulations and make corrections as necessary to become compliant.

Management’s Response and Corrective Action Plan

DVA does not have authority or internal control as far as it concerns the construction process of the cemetery. The finance cabinet controls the contract and all purchases and change orders that are involved in the construction phase of the SCG program. Although, during the construction phase of the SCG program, there is at a minimum a monthly progress meeting which KDVA has a representative attend each one of these meetings. We have attached a copy of each of these monthly meeting minutes to this memo, which show that there is a

**COMMONWEALTH OF KENTUCKY
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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DVA2-36: The Kentucky Department of Veterans Affairs Should Monitor Grant Supported Activities to Assure Compliance With Applicable Federal Requirements (Continued)

Management's Response and Corrective Action Plan (Continued)

representative of KDVA at each one of these meetings. These notes are also forwarded to the Commissioner of KDVA and the Branch Manager of the cemeteries, which is shown in the notes. KDVA keeps abreast of all construction issues and expenditures. When purchasing equipment for the cemetery we ensures that purchases met Federal program requirements. For future grants of this nature we will work closely with the finance cabinet to ensure we have more control over the grant. However this may take some sort of legislative change for the finance cabinet to allow us this type of control because the construction process is completely under their purview.

Auditor's Reply

We do not believe a legislative change would be necessary for KDVA to monitor grant-supported activities for compliance with Federal program requirements.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-JUST1-37: The Justice Cabinet Should Implement And Follow An Approved Indirect Cost Allocation Plan

State Agency: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.575--Crime Victim Assistance

CFDA 16.579--Byrne Formula Grant Program

CFDA 16.588--Violence Against Women Formula Grants

Federal Agency: U.S. Department of Justice - Office of Justice Programs

Pass-Through Agency: Not Applicable

Compliance: Allowable Costs/Cost Principles

Amount of Questioned Costs: \$363,063

Indirect costs are those costs that benefit common activities and, therefore, cannot be readily assigned to a specific direct cost objective or project. As we noted during the FY 2002 and FY 2003 audits, the Justice Cabinet - Office of the Secretary does not have an approved indirect cost plan in place for charging indirect costs to federal grants, indirect costs are included as part of the administrative costs for the agency.

We also noted that while payroll charged to grants is typically a direct charge based on actual hours worked, Justice Cabinet allocates payroll charges to grants indirectly based on percentages determined in a time study prepared several years ago. Justice Cabinet could not provide auditors with any information or support for this time study. Therefore, we could not verify the accuracy or validity of the percentages used.

During FY 2004, Justice Cabinet GMB personnel worked on the indirect cost allocation plan, but did not have one in place. On January 31, 2005, Justice Cabinet submitted an indirect cost plan for approval to the federal cognizant agency. Written approval had not been obtained as of February 28, 2005.

Charging indirect costs to federal grants without an approved indirect cost plan in place is not in compliance with OMB Circular A-133, Compliance Supplement Part 3 - Compliance Requirements, Section B. Allowable Costs/Cost Principles.

OMB Circular A-133 Part 3, Section B. Allowable Costs/Cost Principles states that “In order to recover indirect costs, organizations must prepare cost allocation plans (CAPs) which apply only to state, local and Indian tribal governments or indirect cost rate proposals (IDCRPs) in accordance with the guidelines provided in OMB’s Circulars.”

According to the U.S. Department of Justice Financial Guide, Chapter 17, Indirect Costs, “In order to be reimbursed for indirect costs, a recipient must first establish an appropriate indirect cost rate. To do this, the recipient must prepare an indirect cost rate proposal and submit it to the cognizant Federal agency . . . If an indirect cost proposal for

**COMMONWEALTH OF KENTUCKY
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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-JUST1-37: The Justice Cabinet Should Implement And Follow An Approved Indirect Cost Allocation Plan (Continued)

recovery of actual indirect costs is not submitted to the cognizant Federal agency within three months of the start of the award period, indirect costs will be irrevocably lost for all months prior to the month that the indirect cost proposal is received. This policy is effective for all awards.”

Since the agency did not have an approved indirect cost plan in place for FY 2004, we are questioning \$363,063 in costs charged to the three grants included in this audit. Included in this amount are all payroll charges for the three grants, based on the fact that all payroll was charged indirectly using a time study that could not be confirmed.

Recommendation

We recommend that after the indirect cost plan is approved by the federal cognizant, the Justice Cabinet-Office of the Secretary apply the rate consistently to accurately charge indirect costs to grants. If the indirect cost plan is not approved, we recommend that the Justice Cabinet revise the plan to meet federal standards.

We recommend that Justice Cabinet return these questioned costs to the U.S. Department of Justice.

Management’s Response and Corrective Action Plan

The Justice and Public Safety Cabinet acknowledge the need to update time allocations, and Grants Management Branch staff will complete an updated time study by the end of FY2005. However, the Cabinet disagrees with the finding’s interpretation of indirect costs as they apply to staff directly employed by Grants Management Branch and assigned to administer individual grants. Personnel (and related) costs for Grants Management Branch employees were charged as direct administrative costs, not as indirect costs. Although employees’ time allocations must be updated (as recognized above), these employees have no responsibilities outside of the branch, and thus their related expenses may, indeed, be “readily assigned to specific projects.” Affected Office of the Secretary staff have too diverse responsibilities to track separately, and therefore were considered separately in the Indirect Cost Rate proposal draft recently submitted to the U.S. Department of Justice. We have contacted USDOJ for guidance and will follow their directives to dispose of previously applied and/or future indirect costs and the submitted Indirect Cost Rate proposal.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-JUST1-37: The Justice Cabinet Should Implement And Follow An
Approved Indirect Cost Allocation Plan (Continued)**

Auditor's Reply

We reaffirm that while payroll charged to grants is typically a direct charge based on actual hours worked, the Justice Cabinet allocates payroll charges to grants indirectly based on percentages determined in a time study prepared several years ago. Because the percentages cannot be proven as an accurate reflection of time spent working on a specific grant, these payroll charges are indirect costs for FY 2004.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-JUST2-38: The Justice Cabinet Should Provide Sufficient Documentation Of Subrecipient Monitoring Activities

State Agency: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.575--Crime Victim Assistance

CFDA 16.579--Byrne Formula Grant Program

CFDA 16.588--Violence Against Women Formula Grants

Federal Agency: U.S. Department of Justice - Office of Justice Programs

Pass-Through Agency: Not Applicable

Compliance: Subrecipient Monitoring

Amount of Questioned Costs: None

In the Crime Victim Assistance (VOCA) and Violence Against Women (VAWA) subrecipient files that we reviewed for the 2004 fiscal year audit, there were several instances of files with neither financial nor programmatic monitoring tools completed during the fiscal year. In addition, we noted quarterly subgrantee progress, financial reports and closeout reports were not submitted timely to Grants Management Branch (GMB) by subrecipients. We also noted that payments to subrecipients were often delayed for several months. According to GMB, these payments were delayed due to either late quarterly reports from subrecipients or problems within the quarterly reports submitted by subrecipients.

In the Byrne subrecipient files that we reviewed for the 2004 fiscal year, the auditor noted only two of the ten subrecipients submitted timely financial reports. In addition, there were financial reports received several months past the due date, causing payments to be delayed for these entities. We also noted no financial site visits and only two performance site visits documented.

Without adequate documentation in the subrecipient files, it is not possible to determine what monitoring activities are performed or how often they are performed. It is also difficult to determine why payments have been delayed.

During the 2004 fiscal year, sufficient monitoring activities were not being performed and/or documented to ensure that subrecipients were using Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals were achieved. Subrecipients could be in noncompliance with federal requirements and grant funds could be spent erroneously when monitoring is not performed adequately or timely.

According to OMB Circular A-133, Subpart D (d) Pass-through entity responsibilities, "A pass-through entity shall perform the following for the federal awards it makes: . . .

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-JUST2-38: The Justice Cabinet Should Provide Sufficient Documentation Of Subrecipient Monitoring Activities (Continued)

(3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.”

Policy and procedures for subrecipient monitoring should be in place and followed to ensure subrecipients are spending federal grant funds in compliance with their grant agreement as well as federal laws and regulations.

Recommendation

While GMB has developed a monitoring schedule to determine which subrecipients will receive desk, telephone or site monitoring reviews, we found that the subrecipient files often did not contain documentation that a review had been done. In several cases where payments to subrecipients were delayed, GMB personnel indicated that there had been discrepancies in the quarterly financial report from the subrecipient that needed to be reviewed further. We recommend that GMB thoroughly document these instances in the future within the subrecipient file to support the delay in payment to the subrecipient and that GMB endeavor to ensure timely payments to subrecipients.

We recommend that the GMB continue to implement policies and procedures to ensure that subrecipient monitoring activities are being performed consistently and on a regular basis. We further recommend that documentation of these activities be filed in the subrecipient files when performed.

Management’s Response and Corrective Action Plan

As noted, the Grants Management Branch has made significant improvements in its file maintenance procedures; however, it recognizes the potential for additional improvements. In order to assure the completeness of its records, a random file audit procedure will be established to assure the presence of required documents, or a sufficient explanation for their absence. Fiscal staff have increased their efforts regarding completeness and accuracy of financial reports submitted, and, during the preceding fiscal year, began returning deficient reports to the responsible subgrantee for correction, rather than attempting to resolve matters in-house. Improving documentation of deficiencies and resulting delays will be an area of attention in random file audits, and a focus of fiscal staff.

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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-JUST3-39: The Justice Cabinet Should Monitor Grant Funds Passed-Thru To Other State Agencies For Compliance With Grant Requirements

State Agency: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.579--Byrne Formula Grant Program

Federal Agency: U.S. Department of Justice - Office of Justice Programs

Pass-Through Agency: Not Applicable

Compliance: Allowable Costs/Cost Principles

Amount of Questioned Costs: \$388.25

During testing of payroll expenditures charged to the Byrne Grant for FY 2004 we found that the State Police charged the grant incorrectly for overtime not worked based on the post's payroll summary due to a data entry error. We also found that the Administrative Office of the Courts paid an employee for work completed on a non-grant activity on September 1, 2003 and also for holiday pay from grant funds for the same day. The employee should have only received pay for the non-grant activity and no charges should have been made to the grant for that date.

State Police charged the Byrne Formula Grant by \$179.20. While the Human Resources Department has internal controls in place that found the error and corrected the employee's pay in the following pay period, there were not controls in place to ensure that this error was communicated with the grant accountant so that the charges to the grant could be corrected as necessary. When questioned by the auditor an employee of the payroll department stated, and the Human Resources director concurred, that there is not a procedure in place to communicate these types of errors with the grant accountant. Without notification from Human Resources, the grant accountant could not of been aware of the necessary corrections.

The Administrative Office of the Courts improperly charged the Byrne Grant \$209.05 for non-grant related work the employee performed on September 1, 2003. Policies/procedures in place during the audit period permitted an employee to be improperly paid twice for work on the same day.

OMB A-87 11. h. 4. states, "Where employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports or equivalent documentation . . ."

Recommendation

The Justice Cabinet should consider improving changes to their review of grant funds passed thru to state agencies, including testing samples of time sheets and other expenditure documents, to ensure that funds have been spent in compliance

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-JUST3-39: The Justice Cabinet Should Monitor Grant Funds Passed-Thru To Other State Agencies For Compliance With Grant Requirements (Continued)

Recommendation (Continued)

with federal guidelines, agency grant agreement, and approved budget. Further they should follow-up on known questioned costs herein to ensure that the improper charges have been repaid.

The State Police should strengthen internal controls to prevent the data entry errors, which led to the overcharges as well as improve communications between the Human Resource Department and grants accountant so that errors can be properly corrected in a timely manner. State Police should reimburse the grant for known questioned costs to ensure the improper charges have been repaid.

The AOC internal controls should be strengthened to prevent improper charges to the federal grant. AOC should reimburse the grant for known questioned costs to ensure the improper charges have been repaid.

Management's Response and Corrective Action Plan

Grants Management Branch will direct state agency subgrantees as indicated above, and will continue to enhance monitoring efforts in this, as in other, areas. Subgrantees referenced here will be directed to return the questioned amounts to Grants Management Branch. In the past, the two referenced agencies have submitted extensive documentation for all subgrants awarded to them, with errors infrequently noted. When costs have been questioned, however, they have responded timely.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
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(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-JUST4-40: The Justice Cabinet Should Implement Procedures To Ensure All Grant Funds Are Expended In Accordance With Federal Guidelines

State Agency: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.575--Crime Victim Assistance

CFDA 16.579--Byrne Formula Grant Program

CFDA 16.588--Violence Against Women Formula Grants

Federal Agency: U.S. Department of Justice - Office of Justice Programs

Pass-Through Agency: Not Applicable

Compliance: Allowable Costs/Cost Principles

Amount of Questioned Costs: None

The Justice Cabinet's monitoring of grant expenditures is not sufficient to ensure that grant funds are expended in accordance with grant requirements. In FY04, Byrne Formula Grant expenditures totaled \$6,189,388.40, with \$2,613,100 sent to subrecipients. Besides subrecipients, several state agencies receive Byrne grant funds, including Kentucky State Police (FY04 expenditures \$1,561,504) and Administrative Office of the Courts (FY04 expenditures \$1,221,550). The Justice Cabinet Office of the Secretary had expenditures of \$541,133 including payroll and administrative expenditures.

These funds receive little oversight from the Justice Cabinet Grants Management Branch. There is insufficient monitoring of expenditures made for administrative items. Because of the lack of monitoring, items such as employee retirement plaques were charged to grants.

A significant amount of grant expenditures are made within the Justice Cabinet and within other state agencies, such as State Police and Administrative Office of the Courts. Lack of monitoring of these expenditures leaves a large amount of grant funds without proper monitoring and subject to misappropriation.

OMB Circular No. A-87 Attachment A General Principles for Determining Allowable Costs, A) Purpose and Scope 2. Policy states "... (1) Governmental units are responsible for the efficient and effective administration of Federal awards through the application of sound management practices. (2) Governmental units assume responsibility for administering Federal funds in a manner consistent with underlying agreements, program objectives, and the terms and conditions of the Federal award."

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-JUST4-40: The Justice Cabinet Should Implement Procedures To
Ensure All Grant Funds Are Expended In Accordance With Federal Guidelines
(Continued)**

Recommendation

We recommend that the Justice Cabinet, Office of the Secretary implement procedures to ensure that all grant funds are expended in accordance with federal guidelines. We further recommend that Grants Management Branch apply the same standards to other state agencies, as well as within the Justice Cabinet that they require subrecipients to submit timely reports with sufficient supporting documentation of expenditures. We further recommend that expenditures, including administrative expenditures, be reviewed for allowability based on the requirements of each grant.

Management's Response and Corrective Action Plan

In the past, funds administered by the Office of the Secretary were allowed greater latitude, in terms of reporting, due to resource demands limiting available staff. This resulted in both delayed reporting on some occasions, and a related delay in identifying questionable costs. Recent and upcoming staffing additions in Grants Management Branch and the Office of the Secretary will allow enhanced oversight, along with other general improvements. In addition, improved internal reporting and review controls (e.g, monthly reviews of administrative expenditures by Grants Management Branch's fiscal Internal Policy Analyst III and Branch Manager and the Office of the Secretary's Budget Director and Fiscal Manager) will be in place by May 2005.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
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(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-JUST5-41: The Justice Cabinet Should Not Supplant State Funds With Federal Funds

State Agency: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.579--Byrne Formula Grant Program

Federal Agency: U.S. Department of Justice - Office of Justice Programs

Pass-Through Agency: Not Applicable

Compliance: Matching/Level of Effort/Earmarking

Amount of Questioned Costs: \$30,413

Supplanting means to deliberately reduce State or local funds because of the existence of Federal funds. For example, when State funds are appropriated for a stated purpose and Federal funds are awarded for that same purpose, the State replaces its State funds with Federal funds, thereby reducing the total amount available for the stated purpose.

The Justice Cabinet, Office of the Secretary created a new office, the Office of Investigations in July 2004. Staffing for this office was already in place and being paid with general fund money before the Byrne grant was awarded for this office. The Byrne Grant funds were awarded to the Office of Investigations on September 23, 2004. On November 15, 2004, \$30,413 in payroll for the Office of Investigations staff was charged to the Byrne grant. This included payroll from the 7/31/04 pay period through the 9/30/04 pay period for three Office of Investigations staff members.

By transferring charges to the grant that were already expended as payroll for staff already at work, the Justice Cabinet is supplanting federal funds.

According to the Catalog of Federal Domestic Assistance, the Byrne Formula Grant specifically “restricts the use of these funds for supplanting State and local funds...”

The Edward Byrne Memorial State and Local Law Enforcement Assistance Program Formula Grant Program requirements state “A grant recipient may not use federal grant funds to defray any costs that the recipient is already obligated to pay.”

The US Department of Justice Financial Guide Chapter 16 Unallowable Costs - Costs Incurred Outside the Project Period states “Any costs that are incurred either before the start of the project period or after the expiration of the project period are not allowable.”

Recommendation:

We recommend that Justice Cabinet reimburse the Byrne Grant for the above-mentioned expenditures. We further recommend that Justice Cabinet thoroughly review grant requirements to ensure they are in compliance with all federal grant regulations.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-JUST5-41: The Justice Cabinet Should Not Supplant State Funds
With Federal Funds (Continued)**

Management's Response and Corrective Action Plan

As originally proposed in the Justice and Public Safety Cabinet's reorganization enacted by Executive Order in 2004, the Office of Investigations had a different form, function, scope, and level of authority than the abolished Internal Investigations Branch. Relying on documentation and assurances submitted by the Office of the Secretary to this effect, a Byrne grant was awarded to partially support the operations of the new program. (Administrative staff resource limitations caused the award to be made on a delayed basis due to Grants Management Branch requests for additional application documentation.) However amendments to the Justice and Public Safety Cabinet's Reorganization Bill in the House and Senate during the 2005 session of the General Assembly greatly altered its proposed authority. Due to the revised structure for this program anticipated to be enacted by the General Assembly, the Justice and Public Safety Cabinet will terminate this grant and pay back all expenditures to the Byrne grant. In future, Office of the Secretary grant applications will be held to stricter timeliness requirements.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-NREPC1-42: The Division Of Abandoned Mine Lands Should Take Steps To Ensure That Subrecipient Audit Reports Are Received Within Nine Months Of The Subrecipient’s Year-end And Should Issue Management Decisions On These Reports Within Six Months Of Their Receipt

State Organization: Natural Resources and Environmental Protection Cabinet

Federal Program: CFDA 15.252 –Abandoned Mine Land Reclamation (AMLR) Program

Federal Agency: U.S. Department of the Interior

Pass-Through Agency: Not Applicable

Compliance Area: Subrecipient Monitoring

Amount of Questioned Costs: None

During testing, we examined audit reports for all subrecipients required by Circular A-133 to have an audit. Of the seven audit reports required to be submitted, only two were submitted and reviewed within the nine month required timeframe. Of the remaining five audit reports, one was submitted late, another was completed timely but not obtained timely by the agency, and the remaining three were not submitted and were likely not performed as of the test date. In addition, we noted that there were two instances where reports were received, but were not reviewed within the six month required timeframe.

Although the agency might have been in compliance with obtaining and reviewing audit reports timely in the past, they are not in compliance with the current Circular A-133 requirements.

Office Of Management and Budget (OMB) Circular A-133 in part 3 section M states the following:

“A pass-through entity is responsible for:

Subrecipient Audits - (1) Ensuring that subrecipients expending \$300,000 (\$500,000 for fiscal years ending after December 31, 2003 as provided in OMB Circular A-133, as revised) or more in Federal awards during the subrecipient’s fiscal year have met the audit requirements of OMB Circular A-133 and that the required audits are completed within 9 months of the end of the subrecipient’s audit period, (2) issuing a management decision on audit findings within 6 months after receipt of the subrecipient’s audit report, and (3) ensuring that the subrecipient takes timely and appropriate corrective action on all audit findings. In cases of continued inability or unwillingness of a subrecipient to have the required audits, the pass-through entity shall take appropriate action using sanctions.”

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-NREPC1-42: The Division Of Abandoned Mine Lands Should Take Steps To Ensure That Subrecipient Audit Reports Are Received Within Nine Months Of The Subrecipient’s Year-end And Should Issue Management Decisions On These Reports Within Six Months Of Their Receipt (Continued)

Recommendation

We recommend that the Natural Resources and Environmental Protection Cabinet (NREPC) perform the following:

- Notify each subrecipient about the subrecipient audit requirement described above.
- The agency should consider sending a reminder notice 5 months after the end of the subrecipient’s fiscal year.
- When a subrecipient fails to submit the required audit report within 9 months of the end of the subrecipient’s audit period, the agency should mail a notice via certified mail with return receipt stating that the audit report required is delinquent. Further, Section 225 Subpart B of Circular A-133 states, “In cases of continued inability or unwillingness to have an audit conducted in accordance with this part, Federal agencies and pass-through entities shall take appropriate action using sanctions such as: a) withholding a percentage of Federal awards until the audit is completed satisfactorily; b) withholding or disallowing overhead costs; c) suspending Federal awards until the audit is conducted; or d) terminating the Federal award.”
- Finally, the agency should ensure that the management decision on audit findings is issued within six months after receipt of the subrecipient’s audit report.

Management’s Response and Corrective Action Plan

We notify subrecipients of the audit requirement in their agreement. A reminder letter is normally sent four months in advance, however, we missed our deadlines this year due to an increased workload with the reorganization.

Of the five audits that had not been received, four audits were due from county governments. Three of those four were performed by the Auditor of Public Accounts (APA) and the fourth was completed by an independent firm and is being reviewed by APA before release. Because the county governments are

COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
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(CONTINUED)

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-NREPC1-42: The Division Of Abandoned Mine Lands Should Take Steps To Ensure That Subrecipient Audit Reports Are Received Within Nine Months Of The Subrecipient’s Year-end And Should Issue Management Decisions On These Reports Within Six Months Of Their Receipt (Continued)

Management’s Response and Corrective Action Plan (Continued)

required by statute to use the Auditor of Public Accounts, it seemed unfair to levy any sanctions upon them or send out notices caused by another Commonwealth agency. However, in order to comply with your recommendations and Circular A-133, we will be sending out a certified letter to the three that remain outstanding.

Auditor’s Reply

We agree that NREPC notifies subrecipients of their audit requirements, however, the notification provided states that audit reports are due within thirteen months of the subrecipient’s year-end whereas Circular A-133 requires that these reports be submitted within nine (9) months. Therefore, future MOAs should be updated to ensure the agency and subrecipients are in compliance with this section of the Circular A-133 requirements.

Circular A-133 governs federal awards. Although the agency does not believe it would be fair to sanction the subrecipients for not having audits completed timely, Circular A-133 is very clear on the agency’s responsibility as a pass-through entity of federal awards. Part 225 of Circular A-133 states (emphasis was added by the APA):

In cases of continued **inability** or unwillingness to have an audit conducted in accordance with this part, Federal agencies and pass-through entities **shall** take appropriate action using sanctions such as:

- (a) Withholding a percentage of Federal awards until the audit is completed satisfactorily;
- (b) Withholding or disallowing overhead costs;
- (c) Suspending Federal awards until the audit is conducted; or
- (d) Terminating the Federal award.

This section states that pass-through entities shall (not could or should) implement sanctions in instances when subrecipients are unable to comply with the Circular A-133 requirements.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING: 04-NREPC1-42: The Division Of Abandoned Mine Lands Should Take Steps To Ensure That Subrecipient Audit Reports Are Received Within Nine Months Of The Subrecipient's Year-end And Should Issue Management Decisions On These Reports Within Six Months Of Their Receipt (Continued)

Auditor's Reply (Continued)

We acknowledge the APA was engaged to perform some of the audits mentioned above and our office recognizes its responsibility under state statutes and federal guidelines. Unfortunately, the timely completion of local government audits is contingent on a number of factors. The APA is working closely with local governments to expedite the completion of audits, especially those receiving federal funds.

We further acknowledge that the agency is performing other administrative functions - reporting, site visits, and regular contacts - related to monitoring that would help mitigate the effects of not having audit reports submitted in a timely fashion. The pass-through entity should also advise subrecipients they may request and receive extensions related to the submission of audits.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-TC9-43: The Transportation Cabinet Should Improve The Change Order Process

State Agency: Transportation Cabinet

Federal Program: 20.205 – Highway Planning and Construction

Federal Agency: Not Applicable

Pass-Through Agency: U.S. Department of Transportation

Compliance Area: Allowable Costs/Cost Principles

Amount of Questioned Cost: None

During our audit of the Transportation Cabinet, a draft report prepared by the Cabinet's Office of Inspector General (OIG) heightened our awareness of a situation present within the cabinet. Within this report, it was disclosed that Cabinet policies in regards to change orders were "blatantly ignored." None of the five projects mentioned within the report involved federal funds; however, if Federal Funds had been utilized, questioned cost may have arisen for these expenditures.

Our audit of the Highway Planning and Construction program noted that a total of 16 change orders were observed for one project during FY 04. Within the project file, a total of 38 change orders were observed. Numbering of change orders suggest that as many as 48 were processed over the life of the project, which appears to be excessive. During our audit, it was observed that a total of thirteen projects originally awarded a total of \$214.8 million were increased by \$12.5 million in change orders.

The Cabinet OIG disclosed that 1087 change orders were approved during FY 04.

Allowing use of multiple change orders during projects demonstrates that there is inefficient planning conducted and allows the Commonwealth to be susceptible to instances of bid-rigging and instances of fraud.

OMB Circular A-133 Part 6 states, "The A-102 Common Rule and OMB Circular A-110 require that non-Federal entities receiving Federal awards (i.e., auditee management) establish and maintain internal control designed to reasonably ensure compliance with Federal laws, regulations, and program compliance requirements."

**COMMONWEALTH OF KENTUCKY
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(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-TC9-43: The Transportation Cabinet Should Improve The Change Order Process (Continued)

Recommendation

The APA noted during our review of the draft report of the OIG preliminary recommendations, which should be considered for implementation. Some of them are:

- “More oversight given in the use of Change orders...”
- “The use of Lump Sum Change Orders should be avoided and used only in extreme circumstances...”
- “Existing and future policy set in place to govern Change orders must be strictly enforced...”
- “Contractors who are awarded bid contracts should be, if at all possible, held to their original winning bid...”
- “ If major Change Orders address the Design of a project, the Design Division should have input as to the necessity of the change, and should be included in the approval process...”
- Disagreements “should be noted by Memorandum, and attached to the Change order before it proceeds to next level...”

In addition, we recommend that:

- The Cabinet consider adopting new policies for design and planning that could possibly extinguish, or significantly reduce the use of change orders. Hold contractors to original winning bid as suggested by the Cabinet OIG.

Our office is currently working with the Federal Highway Administration in the Kentucky Transportation Cabinet (KYTC) OIG, to review change orders, as part of a broader review.

Management’s Response and Corrective Action Plan

The Transportation Cabinet recognizes the need for a system that maintains internal controls and compliance with all Federal and State laws, regulations and program compliance requirements. The Cabinet is currently implementing new contract management software (Transport; Site Manager), which was developed by the American Association of State Highway & Transportation Officials (AASHTO) and has been customized for Kentucky needs. This software will be fully implemented by June 30, 2005.

COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
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(CONTINUED)

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-TC9-43: The Transportation Cabinet Should Improve The Change Order Process (Continued)

Management's Response and Corrective Action Plan (Continued)

Specific responses to items in the recommendation are:

- *"More oversight given in the use of Change orders..." **The Cabinet has increased the scrutiny of all change orders.***
- *"The use of Lump Sum Change Orders should be avoided and used only in extreme circumstances..." **Lump sum change orders are used sparingly and detailed records are maintained.***
- *"Existing and future policy set in place to govern Change orders must be strictly enforced..." **The existing policy is being strictly enforced.***
- *"Contractors who are awarded bid contracts should be, if at all possible, held to their original winning bid..." **While not always possible every effort is made to limit the number of change orders.***
- *"If major Change Orders address the Design of a project, the Design Division should have input as to the necessity of the change, and should be included in the approval process..." **This policy has been in place for approximately three years.***
- *disagreements "should be noted by Memorandum, and attached to the Change order before it proceeds to next level..." **SiteManager will allow comments to become part of the change order record.***
- *The Cabinet should consider adopting new policies for design and planning that could possibly extinguish, or significantly reduce the use of change orders. **This is already in place with our "Lessons Learned Database"***
- *Hold contractors to original winning bid as suggested by the Cabinet OIG. **While not always possible every effort is made to limit the number of change orders.***

With the implementation of the new software, Construction employees have received countless hours of training that will further strengthen the staff's ability to follow the procedures to ensure full compliance with necessary audit requirements.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
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(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-TC10-44: The Transportation Cabinet Should Improve Procedures To Ensure Federal Reports Are Submitted Timely

State Agency: Transportation Cabinet

Federal Program: 20.500 and 20.509 – Federal Transit – Formula Grants; Formula Grants for Other Than Urbanized Areas

Federal Agency: U. S. Department of Transportation

Pass-Through Agency: Not Applicable

Compliance Area: Reporting

Amount of Questioned Cost: None

OMB Circular A-110 subpart C section .52(a)(1)(i) states “Each Federal awarding agency shall require recipients to use the SF269 or SF269A to report the status of funds for all non-construction projects or programs.” During our audit of the Transportation Cabinet, thirty federal financial status reports were reviewed for timely submission. Out of the thirty reports reviewed, sixteen were submitted between five and forty days late.

Lack of compliance with the required submission dates could result in federal assistance being reduced or possibly suspended.

OMB Circular A-110 subpart C section .52 states, “(iv) The Federal awarding agency shall require recipients to submit the SF-269 or SF-269A (an original and no more than two copies) no later than 30 days after the end of each specified reporting period for quarterly and semi-annual reports, and 90 calendar days for annual and final reports. Extensions of reporting due dates may be approved by the Federal awarding agency upon request of the recipient.”

Recommendation

The Transportation Cabinet should strive to submit Federal Financial Status Reports within the deadlines or make formal written requests for extensions.

Management’s Response and Corrective Action Plan

During the audit review, the auditor requested a federal time extension for the SF 269 reports with late submissions (July 2003-March 2004).

Please note that the Federal Transit Administration (FTA) accepted the reports with the submittal dates and the Transportation Cabinet was not cited for non-compliance with reporting requirements. The federal acceptance indicates no ramifications nor did it cause a reduction in funding.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-TC10-44: The Transportation Cabinet Should Improve Procedures
To Ensure Federal Reports Are Submitted Timely (Continued)**

Management’s Response and Corrective Action Plan (Continued)

However, to get an official statement for the Auditor, staff from the Office of Transportation Delivery called and e-mailed the federal project and requested an extension by e-mail granted the extension for said reports.

As a follow-up, the auditor contacted the Federal Manager and requested further information and the following is the response from the Federal Transit Administration:

“I am a Program Manager within the Division of Operations and Program Management in the Regional FTA Office. With regard to your questions, unless the grantee is a flagrant violator of FTA requirements, FTA will not penalize the grantee for being late in submitting their reports. Normally, we would call or send out letters reminding the grantee that their reports are past due. For flagrant violators there is a possibility that the grant would be closed if the situation does not improve.”

The SF 269 process:

Before you can initiate a grant, a SF 269 report is required. Yet no activity has occurred. To expedite a grant closeout, FTA has accepted the quarterly expenditures along with the final payment the first month following the end of the quarter. This allows for a four month closeout period rather than waiting and having a six month closeout. Therefore, giving a late SF 269-report submission but having an early grant closeout. Additionally, after the final draw down, the FTA Federal Manager can closeout the grant before the State has an opportunity to submit a SF 269 report. This is because FTA can see all of the activities in the federal system along with the financial draws made from the Washington Bank to the respective project.

However, since the Jan-March 2004 quarterly report submissions, the staff of the Office of Transportation Delivery has submitted all reports within the thirty-day recommendation and the schedule is as follows:

**COMMONWEALTH OF KENTUCKY
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(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-TC10-44: The Transportation Cabinet Should Improve Procedures To Ensure Federal Reports Are Submitted Timely (Continued)

Management's Response and Corrective Action Plan (Continued)

SF 269 Reports Quarterly Schedule TC/Office of Transportation Delivery								
<i>Grant</i>	<i>Grant #</i>	<i>FFY</i>	<i>SFY</i>	<i>Calendar</i> <i>Year</i>	<i>Month</i>	<i>QTR</i> <i>FFY</i>	<i>Date</i> <i>Due</i>	<i>Date</i> <i>Submitted</i>
KY-03	0046	05	05	2004	October-December	1st	1/30/05	1/25/2005
KY-03	0050	05	05	2004	October-December	1st	1/30/05	1/26/2005
KY-03	0054	05	05	2004	October-December	1st	1/30/05	1/26/2005
KY-03	0063	05	05	2004	October-December	1st	1/30/05	1/26/2005
KY-03	0066	05	05	2004	October-December	1st	1/30/05	1/4/2005
KY-16	0031	05	05	2004	October-December	1st	1/30/05	1/28/2005
KY-18	0022	05	05	2004	October-December	1st	1/30/05	1/28/2005
KY080	X12	05	05	2004	October-December	1st	1/30/05	1/28/2005
KY080	X13	05	05	2004	October-December	1st	1/30/05	1/28/2005
KY-03	0046	04	05	2004	July-September	4th	10/30/05	10/25/2004
KY-03	0054	04	05	2004	July-September	4th	10/30/05	10/25/2004
KY-16	0031	04	05	2004	July-September	4th	10/30/05	10/27/2004
KY-18	0021	04	05	2004	July-September	4th	10/30/05	10/27/2004
KY-18	0022	04	05	2004	July-September	4th	10/30/05	10/27/2004
KY-90	X138	04	05	2004	July-September	4th	10/30/05	10/27/2004
KY-90	X140	04	05	2004	July-September	4th	10/30/05	10/27/2004
KY080	X11	04	05	2004	July-September	4th	10/30/05	10/29/2004
KY080	X12	04	05	2004	July-September	4th	10/30/05	10/27/2004
KY-03	0038	04	04	2004	April-June	3rd	7/30/04	7/8/2004
KY-03	0046	04	04	2004	April-June	3rd	7/30/04	7/8/2004
KY-03	0047	04	04	2004	April-June	3rd	7/30/04	7/8/2004
KY-03	0048	04	04	2004	April-June	3rd	7/30/04	7/8/2004
KY-03	0050	04	04	2004	April-June	3rd	7/30/04	7/26/2004
KY-03	0054	04	04	2004	April-June	3rd	7/30/04	7/26/2004
KY-16	0030	04	04	2004	April-June	3rd	7/30/04	7/26/2004
KY-16	0031	04	04	2004	April-June	3rd	7/30/04	7/26/2004
KY-90	X138	04	04	2004	April-June	3rd	7/30/04	7/26/2004
KY080	X11	04	04	2004	April-June	3rd	7/30/04	7/26/2004
KY080	X12	04	04	2004	April-June	3rd	7/30/04	7/26/2004
KY-18	0021	04	04	2004	April-June	3rd	7/30/04	7/26/2004
KY-18	0022	04	04	2004	April-June	3rd	7/30/04	7/26/2004

**COMMONWEALTH OF KENTUCKY
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SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-TC10-44: The Transportation Cabinet Should Improve Procedures
To Ensure Federal Reports Are Submitted Timely (Continued)**

Management's Response and Corrective Action Plan (Continued)

If you follow the strict thirty day period submission and a grant nears closeout, the grant closeout could be delayed and the FTA Manager may initiate closeout on the federal side.

In summation, the Office of Transportation Delivery staff shall continue to submit the Federal Financial Status Reports within the deadlines or make a formal request for extension in order to expedite grant closeouts. The reports will be electronically submitted by the Staff Assistant and the Administrative Specialist III will maintain the schedule denoting the submittal dates.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-TC11-45: The Transportation Cabinet Should Improve Procedures
To Ensure Federal Reports Are Prepared Accurately**

State Agency: Transportation Cabinet
Federal Program: 20.205 - Highway Planning and Construction
Federal Agency: U.S. Department of Transportation
Pass-Through Agency: Not Applicable
Compliance Area: Reporting
Amount of Questioned Cost: None

The Transportation Cabinet is responsible for submitting an “Office of Real Estate Services Annual Program Statistics” to the regional Federal Highway Administration (FHWA) each federal fiscal year. We tested the FY04 Report and found several discrepancies. There were numerous totals on the report that did not agree to supporting documentation. These were not major discrepancies, however, they were not accurate. This report is often times electronic, however, this year, FHWA did not provide an electronic version. TC simply submitted a handwritten report to FHWA with no transmittal letter. The report submitted lacked the Division, Date of Report and reporting period. The auditor had to contact the FHWA to determine when the report was submitted. We also found that amounts recorded within the report were inaccurate.

Great improvements have been made by the Division of Right of Way and Utilities with this report. Recommendations from our FY03 audit have been put in place accordance with TC’s corrective action plan. However, it appears that management is not performing an in-depth review of this report.

49 CFR subpart 24, Appendix B states “Submit an original and two copies of this report to (Name and Address of Federal Agency) as soon as possible after September 30, but NOT LATER THAN NOVEMBER 15.” This report was not submitted until January 10, 2005, which is 3 months late.

Recommendation

We recommend the Division of Right of Way and Utilities develop policies and procedures for checking figures reported in the statistical report. We also recommend that the report be complete, accurate, reviewed and accompanied by a transmittal letter or dated report.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-TC11-45: The Transportation Cabinet Should Improve Procedures
To Ensure Federal Reports Are Prepared Accurately (Continued)**

Management's Response and Corrective Action Plan (Continued)

A system of codes similar to the one now implemented in the Relocation Branch has been developed for the Acquisition Branch. These codes will be used in the Reporting Category of the MARS funding strip to identify the type of payment being made. This should allow for easier reconciliation of the MARS data and the in house records. This will also help identify any keying errors and enable a correction to be made through a JVB to ensure more accurate reporting. At the suggestion of your office, the Relocation Branch is submitting a revised report. The Division is also in the process of amending it's policy and procedures to reflect an administrative review and timely filing of the annual report.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-TC12-46: The Transportation Cabinet Should Improve Review And Authorization Procedures For Relocation Payments

State Agency: Transportation Cabinet

Federal Program 20.205 – Highway Planning and Construction

Federal Agency: U.S. Department of Transportation

Pass-Through Agency: Not Applicable

Compliance Area: Allowable Costs/Cost Principles; Special Tests & Provisions

Amount of Questioned Cost: None

During our audit testing of relocation expenditures we found that procedures are inadequate to ensure that ‘Payment Summaries’ are authorized by signature of a central office supervisor prior to payment being made to displacees. Specifically, in thirty-five Relocation expenditures examined, a payment of \$1,000 was made to a displacee without first obtaining a signature of a central office supervisor on the ‘Payment Summary’ to authorize the payment

Without proper review and authorization of Relocation payments, disbursement may be made for costs or activities that are unallowed for the Highway Planning and Construction program.

OMB Circular A-133 Part 6 states, “The A-102 Common Rule and OMB Circular A-110 require that non-Federal entities receiving Federal awards (i.e., auditee management) establish and maintain internal control designed to reasonably ensure compliance with Federal laws, regulations, and program compliance requirements.”

An adequate internal control system over disbursements requires that payments be reviewed and authorized by appropriate personnel.

Recommendation

The Right of Way Division should remind supervisors and employees initiating or processing payments to be sure that all applicable signatures or approvals have been obtained and documented in accordance with the Division’s procedures prior to disbursement of funds, reducing the likelihood of the disbursement of funds for costs or activities unallowed.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-TC12-46: The Transportation Cabinet Should Improve Review And
Authorization Procedures For Relocation Payments (Continued)**

Management's Response and Corrective Action Plan (Continued)

The unapproved relocation payment at Central Office level was an oversight. The payment was for a fixed rate move and all documentation was included in the packet. A reminder will be sent to all appropriate personnel regarding the payment approval procedure.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-TC13-47: The Transportation Cabinet Should Ensure FHWA Approval Is Obtained Before Relocation Payments Are Made

State Agency: Transportation Cabinet
Federal Program: 20.205 – Highway Planning and Construction
Federal Agency: U.S. Department of Transportation
Pass-Through Agency: Not Applicable
Compliance Area: Special Tests and Provisions
Amount of Questioned Cost: \$65,129

During our testing of relocation expenditures, we found that there were inadequate procedures in place to ensure that the Federal Highway Administration authorized relocation expenditures on the project agreement (Form PR-1) before relocation payments were made. We found two instances, out of 35 items tested, where relocation expenditures were charged to the federal project, but the project agreement stated that ‘No Relocation’ payments were authorized. Relocation expenditures totaling \$65,129.38 were charged to these two acquisition projects.

Lack of compliance with conditions contained in the project agreement could cause a reduction or suspension of federal assistance.

The A-133 Compliance Supplement states, “Federal funds can be used only to reimburse costs that are in accordance with the conditions contained in the project agreement and the plans, specifications, and estimates” (23 CFR sections 1.9, 630.106 and 630.205).

Recommendation

The Division of Right of Way should remind supervisors and employees initiating or processing payments to be sure that relocation expenditures have been authorized by the FHWA. We recommend that the employee confirm relocation expenditures are in compliance with the project agreement and, if not agreeable, then the employee should inform the Division Director that a request for a redirection of funds is needed.

Management’s Response and Corrective Action Plan

- 1. Met with all parties involved including District and Central Office Staff.*
- 2. Will advise all Right of Way Supervisors by memo to make sure that when relocation is added to a project (that did not originally have relocation), a request will be made to central office programming to add relocation funds.*

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-TC13-47: The Transportation Cabinet Should Ensure FHWA
Approval Is Obtained Before Relocation Payments Are Made (Continued)**

Management's Response and Corrective Action Plan (Continued)

3. *Right of Way programming will provide the Relocation Branch with a copy of the PR-1 at the time of right of way authorization on all projects. This will allow for the Relocation Branch to "double check" for relocation funding.*

COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Material Weaknesses and/or Material Instances of Noncompliance:

FINDING 04-DMA4-48: The Department Of Military Affairs Should Develop An Internal Control System For The State Domestic Preparedness Equipment Assistance Program To Comply With OMB Circular A-133 Compliance Requirements

State Agency: Department of Military Affairs

Federal Program: CFDA 97.004 – State Domestic Preparedness Equipment Support Program

Federal Agency: U.S. Department of Homeland Security

Pass-Through Agency: Not Applicable

Compliance Area: Subrecipient Monitoring

Amount of Questioned Costs: None

The State Domestic Preparedness Equipment Support Program did not establish the following internal control procedures to ensure compliance with the subrecipient monitoring requirements found in OMB Circular A-133, including:

- Advising subrecipients (except for general language in the Memorandum of Agreement) of their responsibility to obtain an audit of Federal awards exceeding \$300,000 in state FY 03 and \$500,000 in state FY 04;
- Establishing a tracking system to determine which subrecipients were required to have an A-133 audit prepared which includes all the required components;
- Establishing a monitoring system to determine if subrecipients have established adequate internal control procedures over Federal awards to ensure federal funds are used for authorized purposes in compliance with laws and regulations;
- Performing desk reviews of A-133 subrecipient audits submitted;
- Resolving audit findings within six months after receipt of the subrecipient audit report and ensuring the subrecipient took timely corrective action;
- Reconciling the amount of Federal awards reported in subrecipient audits to amounts in the MARS accounting system.

State Domestic Preparedness Equipment Support Program has experienced a significant increase in the amount of federal funds received and a corresponding increase in the

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA4-48: The Department Of Military Affairs Should Develop An Internal Control System For The State Domestic Preparedness Equipment Assistance Program To Comply With OMB Circular A-133 Compliance Requirements (Continued)

amount passed through to subrecipients. Military Affairs did not implement procedures to ensure subrecipients complied with the audit and monitoring requirements of OMB Circular A-133.

OMB Circular A-133 Subpart D (d) requires the recipients of federal awards that pass these funds through to subrecipients to implement internal controls for the following areas:

- (1) Identify Federal awards made by informing each subrecipient of CFDA title and number, award name and number, award year, if the award is R&D, and name of Federal agency.
- (2) Advise subrecipients of requirements imposed on them by Federal laws, regulations, and the provisions of contracts or grant agreements as well as any supplemental requirements imposed by the pass-through entity.
- (3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.
- (4) Ensure that subrecipients expending \$300,000 (*\$500,000 for fiscal years ending after December 31, 2003*) or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.
- (5) Issue a management decision on audit findings within six months after receipt of the subrecipient's audit report and ensure that the subrecipient takes appropriate and timely corrective action.
- (6) Consider whether subrecipient audits necessitate adjustment of the pass-through entity's own records.
- (7) Require each subrecipient to permit the pass-through entity and auditors to have access to the records and financial statements as necessary for the pass-through entity to comply with this part.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA4-48: The Department Of Military Affairs Should Develop An Internal Control System For The State Domestic Preparedness Equipment Assistance Program To Comply With OMB Circular A-133 Compliance Requirements (Continued)

Recommendation:

We recommend Military Affairs establish procedures to comply with OMB Circular A-133.

Management's Response and Corrective Action Plan:

Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for sub-recipient monitoring is to provide reasonable assurance that Federal grant award information and compliance requirements are identified to sub-recipients, sub-recipient activities are monitored, sub-recipient audit findings are resolved, the impact of any sub-recipient noncompliance on the pass-through entity is evaluated, and sub-recipients obtained required audits and take appropriate corrective action on audit findings. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.

DMA concurs with the auditor's finding and has developed a corrective action plan designed to restore compliance and insure future compliance.

The Kentucky Division of Emergency Management's State Domestic Preparedness Equipment Support Program, as the federal grantee for the federal grant program, has developed a corrective action plan and has already initiated actions to correct the findings as described below:

- 1. Effective immediately, all KyDEM grant programs, to include the State Domestic Preparedness Equipment Support Program, shall utilize the grant's Master Agreement MARS document to incorporate all federal grant regulatory compliance information, to include OMB Circular A-133 audit and other requirements, is formally and contractually identified for sub-recipient compliance.*

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA4-48: The Department Of Military Affairs Should Develop An Internal Control System For The State Domestic Preparedness Equipment Assistance Program To Comply With OMB Circular A-133 Compliance Requirements (Continued)

Management's Response and Corrective Action Plan (Continued):

2. *KyDEM has already issued written internal division policy #133-1, Sub-Recipient Audits / Monitoring, to establish a divisional monitoring system to determine if sub-recipients have established adequate internal control procedures over Federal awards to ensure federal funds are used for authorized purposes in compliance with laws and regulations. The policy was provided to the auditors.*
3. *Effective the start of state fiscal year 2005 each KyDEM section responsible for the dispersion of federal grant funds, to include the State Domestic Preparedness Equipment Support Program, shall review the audits for their federal program sub-recipients, when received, to comply with OMB Circular A-133 and division policy #113-1, or later approved version. A memo record of this review shall be provided to the KyDEM Assistant Director for each sub-recipient audit reviewed no later than August 31st annually. When applicable, a management decision on the correction / non-correction of a sub-recipient audit finding will be issued the KyDEM Assistant Director within six months after the receipt of the sub-recipient audit report.*
4. *By June 30, 2005, KyDEM shall staff a position using federal administrative cost grant funds to perform desk reviews of sub-recipient audit reports and to work with the sub-recipients to resolve audit findings within six months after receipt of the sub-recipient audit report and ensure the sub-recipient takes timely corrective action.*
5. *At the end of each state fiscal year and upon receipt of sub-recipient audit reports for that year, each KyDEM section responsible for the dispersion of federal grant funds, to include the State Domestic Preparedness Equipment Support Program, shall reconcile the amount of Federal awards reported in sub-recipient audits to amounts in the MARS accounting system for the same CFDA number and period of time as the sub-recipient's audit and a memo record of this reconciliation with supporting MARS financial documents shall be provided to the KyDEM Assistant Director no later than August 31st annually.*

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA5-49: The Department Of Military Affairs Should Follow Established Internal Controls Used To Ensure Compliance With OMB Circular A-133 Compliance Requirements For The Public Assistance Program

State Agency: Department of Military Affairs

Federal Program: CFDA 97.036 – Public Assistance Grants

Federal Agency: U.S. Department of Homeland Security

Pass-Through Agency: Not Applicable

Compliance Area: Subrecipient Monitoring

Amount of Questioned Costs: None

The Public Assistance Program did not establish the following procedures to ensure compliance with many of the audit and monitoring requirements found in OMB Circular A-133, including:

- Advising all subrecipients of their responsibility to obtain an audit of Federal awards exceeding \$300,000 in state FY 03 and \$500,000 in state FY 04;
- Establishing a monitoring system to determine if subrecipients have established adequate internal control procedures over Federal awards to ensure federal funds are used for authorized purposes in compliance with laws and regulations;
- Performing desk reviews of A-133 subrecipient audits submitted;
- Resolving audit findings within six months after receipt of the subrecipient audit report and ensuring the subrecipient took timely corrective action;
- Reconciling the amount of Federal awards reported in subrecipient audits to amounts in MARS accounting system.

Also, we examined the tracking system used by the Recovery Branch to track whether subrecipients had filed A-133 audits, related findings or comments, risk any status of findings and comments. In our testing of the tracking system, we examined 43 subrecipients and noted that 30 were not listed, two were listed stating that DMA did not provide federal assistance and four subrecipients were listed on the tracking device but did not list information applicable to the disaster we were testing.

Also, Military Affairs indicated that all subrecipients of federal awards received letters informing them of their audit responsibilities, whether the audit had been completed,

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA5-49: The Department Of Military Affairs Should Follow Established Internal Controls Used To Ensure Compliance With OMB Circular A-133 Compliance Requirements For The Public Assistance Program (Continued)

whether the audit had findings, and the reasoning for no audit being performed. In our review of 40 public assistance disaster folders we could not locate these letters in 10 instances.

Subrecipient monitoring has been a recurring comment for Military Affairs and in response to these comments, Military Affairs developed detailed procedures to correct past deficiencies. However, these procedures were not implemented until mid December 2004. These procedures were not implemented in time to affect corrections in our audit of state FY 04.

OMB Circular A-133 Subpart D (d) requires the following:

- (1) Identify Federal awards made by informing each subrecipient of CFDA title and number, award name and number, award year, if the award is R&D, and name of Federal agency.
- (2) Advise subrecipients of requirements imposed on them by Federal laws, regulations, and the provisions of contracts or grant agreements as well as any supplemental requirements imposed by the pass-through entity.
- (3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.
- (4) Ensure that subrecipients expending \$300,000 (*\$500,000 for fiscal years ending after December 31, 2003*) or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.
- (5) Issue a management decision on audit findings within six months after receipt of the subrecipient's audit report and ensure that the subrecipient takes appropriate and timely corrective action.
- (6) Consider whether subrecipient audits necessitate adjustment of the pass-through entity's own records.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA5-49: The Department Of Military Affairs Should Follow Established Internal Controls Used To Ensure Compliance With OMB Circular A-133 Compliance Requirements For The Public Assistance Program (Continued)

(7) Require each subrecipient to permit the pass-through entity and auditors to have access to the records and financial statements as necessary for the pass-through entity to comply with this part.

Recommendation:

We recommend Military Affairs:

- Continue to implement the procedures established to fully comply with OMB Circular A-133.
- Improve the tracking devise to include all subrecipients for all disasters.
- Ensure that each subrecipient receives audit letters and that they are placed in each applicable disaster folder. This information is readily available from a report run by the Chief Administrative Officer.

Management's Response and Corrective Action Plan:

Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for sub-recipient monitoring is to provide reasonable assurance that Federal grant award information and compliance requirements are identified to sub-recipients, sub-recipient activities are monitored, sub-recipient audit findings are resolved, the impact of any sub-recipient noncompliance on the pass-through entity is evaluated, and sub-recipients obtained required audits and take appropriate corrective action on audit findings. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.

DMA concurs with the auditor's finding and has developed a corrective action plan designed to restore compliance and insure future compliance.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 04-DMA5-49: The Department Of Military Affairs Should Follow Established Internal Controls Used To Ensure Compliance With OMB Circular A-133 Compliance Requirements For The Public Assistance Program (Continued)

Management's Response and Corrective Action Plan (Continued):

The Kentucky Division of Emergency Management's State Domestic Preparedness Equipment Support Program, as the federal grantee for the federal grant program, has developed a corrective action plan and has already initiated actions to correct the findings as described below:

- 1. Effective immediately, all KyDEM grant programs, to include the Federal Disaster Public Assistance Program, shall utilize the grant's Master Agreement MARS document to incorporate all federal grant regulatory compliance information, to include OMB Circular A-133 audit and other requirements, is formally and contractually identified for sub-recipient compliance.*
- 2. KyDEM has already issued written internal division policy #133-1, Sub-Recipient Audits / Monitoring, to establish a divisional monitoring system to determine if sub-recipients have established adequate internal control procedures over Federal awards to ensure federal funds are used for authorized purposes in compliance with laws and regulations. This division policy is attached.*
- 3. Effective the start of state fiscal year 2005 each KyDEM section responsible for the dispersion of federal grant funds, to include the Federal Disaster Public Assistance Program, shall review the audits for their federal program sub-recipients, when received, to comply with OMB Circular A-133 and division policy #113-1, or later approved version. A memo record of this review shall be provided to the KyDEM Assistant Director for each sub-recipient audit reviewed no later than August 31st annually. When applicable, a management decision on the correction / non-correction of a sub-recipient audit finding will be issued the KyDEM Assistant Director within six months after the receipt of the sub-recipient audit report.*
- 4. By June 30, 2005, KyDEM shall staff a position using federal administrative cost grant funds to perform desk reviews of sub-recipient audit reports and to work with the sub-recipients to resolve audit findings within six months after receipt of the sub-recipient audit report and ensure the sub-recipient takes timely corrective action.*

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 04-DMA5-49: The Department Of Military Affairs Should Follow
Established Internal Controls Used To Ensure Compliance With OMB Circular
A-133 Compliance Requirements For The Public Assistance Program (Continued)**

Management's Response and Corrective Action Plan:

5. *At the end of each state fiscal year and upon receipt of sub-recipient audit reports for that year, each KyDEM section responsible for the dispersion of federal grant funds, to include the Federal Disaster Public Assistance Program, shall reconcile the amount of Federal awards reported in sub-recipient audits to amounts in the MARS accounting system for the same CFDA number and period of time as the sub-recipient's audit and a memo record of this reconciliation with supporting MARS financial documents shall be provided to the KyDEM Assistant Director no later than August 31st annually.*

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions</u>					
<i>(1) Audit findings that have been fully corrected:</i>					
FY 03	03-CFC2-2	The Cabinet For Families And Children Should Ensure All User Accounts On Its Agency Machines Are Necessary	NA	0	Resolved during FY 04.
FY 03	03-CFC6-28	The Cabinet For Families And Children Should Require State Colleges, Universities, And Area Development Districts To Submit An Annual Audit Report	17.253 93.558 93.563 93.575	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 03	03-CFC7-29	The Cabinet For Families And Children Should Discontinue Temporary Assistance For Needy Families Benefits To Recipients Who Have Reached The Sixty-Month Lifetime Limit	93.558	\$8,876	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 03	03-CFC10-31	The Cabinet For Families And Children Should Disburse Child Support Grant Funds In Compliance With Federal Requirements	93.563	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 02	02-CFC12-33	The Cabinet For Families And Children Should Develop A Policy And Procedures Manual To Ensure Subrecipient Monitoring Is Properly Performed	17.253 93.563 93.575	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions (Continued):</u>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY02	02-CFC14-34	The Cabinet For Families And Children Should Monitor Cases Closely So An Ineligible Recipient Does Not Receive Additional Months Of Benefits	93.558	\$2,616	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 01	01-CFC4-38	The Cabinet For Families And Children Should Develop A Policies And Procedures Manual To Ensure Subrecipient Monitoring Is Properly Performed	17.253 93.558 93.563 93.568 93.575 93.596	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 00	00-CFC-12	The Cabinet For Families And Children Should Impose Sanctions On Subrecipients Who Fail To Meet Audit Requirements Set Forth By OMB Circular A-133	93.558 93.563 93.575 93.596	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 03	03-CHS1-11	The Vital Statistics Branch Should Improve Controls Over Assets And Separate Work Tasks	N/A	0	Resolved during FY 04.
FY03	03-CHS2-12	The Vital Statistics Branch Should Take Steps To Reduce The Identity Theft Risks	NA	0	Resolved during FY 04.
FY 02	02-CHS2-14	The Vital Statistics Branch Should Improve Controls Over Assets And Separate Work Tasks	N/A	0	Resolved during FY 04.
FY 02	02-CHS3-15	The Vital Statistics Branch Should Take Steps To Reduce The Identity Theft Risks	NA	0	Resolved during FY 04.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions (Continued):</u>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 01	01-CHS4-13	The Vital Statistics Branch Should Improve Security Over Assets And Segregate Job Duties	N/A	0	Resolved during FY 04.
FY 01	01-CHS6-15	The Vital Statistics Branch Should Take Steps To Prevent Identity Theft	NA	0	Resolved during FY 04.
FY 03	03-CWD1-25	The Division Of Unemployment Insurance Should Perform Reconciliation Of Tax Payments Received By Kentucky Revenue Cabinet To Its Mainframe Program	NA	0	Resolved during FY 04.
FY 03	03-CWD3-27	The Cabinet For Workforce Development Should Strengthen The Security Of Administrator Accounts	NA	0	Resolved during FY 04.
FY 03	03-CWD10-40	The Department For Training And ReEmployment Should Implement Controls Over Monitoring Procedures To Ensure Compliance	NA	0	Resolved during FY 04.
FY 02	02-CWD4-25	The Cabinet For Workforce Development Should Strengthen The Security Of Administrator Accounts	NA	0	Resolved during FY 04.
FY 02	02-CWD12-51	The Department For Training And ReEmployment Should Implement Additional Procedures To Ensure Subrecipient Findings Are Followed Up On In A Timely Manner	17.255 17.258 17.259 17.260	0	Resolved during FY 04.
FY 01	01-CWD3-23	The Cabinet For Workforce Development Should Improve Local Area Network Server Security And Consistently Apply Policies To All Servers	NA	0	Resolved during FY 04.
FY 03	03-FAC3-5	The Finance And Administration Cabinet Should Ensure All User Accounts On Its Agency Machines Are Necessary	N/A	0	Resolved during FY 04.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions (Continued):</u>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 03	03-FAC1-3	The Finance And Administration Cabinet Should Ensure Proper Classification And Categorization Of Investments In The Cash And Investment Note	N/A	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 03	03-FAC4-6	The Finance And Administration Cabinet Should Secure Listings Of User Names And Associated User IDs For Power Users Of The Management Administration And Reporting System	N/A	0	Resolved during FY 04.
FY 03	03-FAC8-10	The Finance And Administration Cabinet Should Track Federal Expenditures For The Jobs And Growth Tax Relief Reconciliation Act in MARS	N/A	0	Resolved during FY 04.
FY 02	02-FAC2-5	The Finance And Administration Cabinet Should Ensure Consistent Classification And Categorization Of Investments In The Cash And Investment Note.	N/A	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 02	02-FAC7-10	The Finance And Administration Cabinet Should Ensure All User Accounts On Its Agency Servers Are Necessary	N/A	0	Resolved during FY 04.
FY 01	01-FAC2-3	The Finance And Administration Cabinet Should Improve Controls Over Preparation Of The Cash And Investment Note	N/A	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions (Continued):</u>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 03	03-JUST3-34	The Justice Cabinet Should Continue to Develop Procedures To Ensure Subrecipients That Expend More Than \$300,000 In Federal Awards In A 12 Month Period Receive An OMB Circular A-133 Audit	16.575 16.579 16.588	0	Resolved during FY 04.
FY 03	03-JUST4-35	The Justice Cabinet Should Ensure Information On The Quarterly Financial Status Report Is Reliable	16.575 16.579 16.588	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 03	03-JUST5-36	The Justice Cabinet Should Implement Its Corrective Action Plan For Weaknesses Noted In Prior Year Regarding Indirect Costs	16.575 16.579 16.588	0	Resolved during FY 04.
FY 02	02-JUST1-39	The Justice Cabinet Should Develop An Indirect Cost Allocation Plan And Submit It To The Cognizant Federal Agency For Approval	16.575 16.579 16.588	N/A	Resolved during FY 04.
FY 02	02-JUST3-41	The Justice Cabinet Should Perform Sufficient Subrecipient Monitoring Activities To Ensure Subrecipients Expending More Than \$300,000 In Federal Awards Receive OMB Circular A-133 Audits	16.575 16.579 16.588	N/A	Resolved during FY 04.
FY 02	02-JUST4-42	The Justice Cabinet Should Prepare Quarterly Financial Status Reports That Are Supported By Adequate Documentation	16.575 16.579 16.588	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 03	03-REV1-13	The Kentucky Revenue Cabinet Should Improve Communication Between Divisions To Ensure Taxpayer Information Is Protected	N/A	0	Resolved during FY 04.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions (Continued):</u>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 03	03-REV2-14	The Kentucky Revenue Cabinet Should Update Its Computer Systems To Remove System Limitations Affecting Accuracy And Reliability Of Reporting	N/A	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 03	03-REV3-15	The Revenue Cabinet Should Strengthen The Security Surrounding Administrator Accounts	N/A	0	Resolved during FY 04.
FY 03	03-REV4-16	The Revenue Cabinet Should Ensure All User Accounts On Its Agency Machines Are Necessary	N/A	0	Resolved during FY 04.
FY 03	03-REV5-17	The Kentucky Revenue Cabinet Should Develop A System For Reconciling Critical Information And Investigating Any Discrepancies	N/A	0	Resolved during FY 04.
FY 02	02-REV1-17	The Kentucky Revenue Cabinet Should Ensure Confidential Taxpayer Information Is Protected And Preserved As Required By Statute	N/A	0	Resolved during FY 04.
FY 02	02-REV2-18	The Kentucky Revenue Cabinet Should Update The Sales Tax Database And Automate Processing Of Accelerated Tax Returns	N/A	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 02	02-REV4-19	The Kentucky Revenue Cabinet Should Strengthen The Security Surrounding Administrator Accounts	N/A	0	Resolved during FY 04.
FY 02	02-REV6-21	The Kentucky Revenue Cabinet Should Ensure All User Accounts On Their Agency Servers Are Necessary	N/A	0	Resolved during FY 04.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions (Continued):</u>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 01	01-REV1-18	The Revenue Cabinet Should Update The Sales Tax Database And Automate Processing Of Accelerated Tax Returns	N/A	0	Due to improvements, this finding is downgraded to an other matter for FY 04. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 01	01-REV3-19	The Revenue Cabinet Should Have A System In Place To Reconcile Critical Information	N/A	0	Resolved during FY 04.
FY03	03-TC1-18	The Transportation Cabinet Should Ensure Adequate Network Level Security Procedures Are Implemented	N/A	0	Resolved during FY 04.
FY03	03-TC2-19	The Transportation Cabinet Should Strengthen The Logical Security Controls Over The Operations Management System	N/A	0	OMS users are not required to change their initial default password when first logging into the system; however, the default password has been changed to a more complex syntax. Comment will be downgraded to a verbal for FY 2004.
FY03	03-TC8-24	The Transportation Cabinet Should Improve Inventory Procedures For Fleet Management	N/A	0	Resolved during FY 04
FY03	03-TC11-38	The Transportation Cabinet Should Obtain Proper Federal Highway Administration Approval Prior To Starting Eligible Federal Assistance Projects	N/A	0	Resolved during FY 04
FY02	02-TC5-49	The Transportation Cabinet Should Obtain Federal Highway Administration Approvals Prior To Granting Authority To Advertise For Projects	20.205	0	Resolved during FY 04

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions (Continued):</u>					
<i>(2) Audit findings not corrected or partially corrected:</i>					
FY 03	03-CFC1-1	The Cabinet For Families And Children Password Policy Should Be Consistently Applied To All Local Area Network Servers	NA	0	Improvements were made during the FY, but issues still exist. See 04-CFC1-1.
FY 03	03-CFC8-30	The Cabinet For Families And Children Should Maintain Adequate Records To Ensure That Payments Are Made For Approved And Allowable Goods And Services	93.558	\$5,791	See 04-CFC6-18 and 04-CFC7-19.
FY 02	02-CFC2-3	The Cabinet For Families And Children's Password Policy Should Be Consistently Applied To All Local Area Network Servers	NA	0	Improvements were made during the FY, but issues still exist. See 04-CFC1-1.
FY 02	02-CFC15-35	The Cabinet For Families And Children Should Maintain And Produce Records To Adequately Support Expenditures	93.558	0	See 04-CFC6-18 and 04-CFC7-19.
FY 01	01-CFC1-1	The Cabinet For Families And Children Should Improve Local Area Network Server Security And Consistently Apply Policies To All Servers	NA	0	See 04-CFC1-1.
FY 01	01-CFC2-36	The Cabinet For Families And Children Should Maintain And Produce Records To Adequately Support Expenditures	93.558	0	See 04-CFC6-18 and 04-CFC7-19.
FY 03	03-CWD11-41	The Department For Training And ReEmployment Should Implement Formal Procedures To Ensure Accurate Federal Reporting	NA	0	See 04-CWD12-28.
FY 03	03-FAC2-4	The Finance And Administration Cabinet Should Strive To Ensure That All State Agencies Conduct Accurate And Timely Fixed Assets Inventory Counts	N/A	0	Not resolved. See 04-FAC3-8

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions (Continued):</u>					
<i>(2) Audit findings not corrected or partially corrected:</i>					
FY 03	03-FAC5-7	The Finance And Administration Cabinet Should Develop And Implement Formal Policy And Procedures To Govern Security Of The Management Administrative And Reporting System Interface Files	N/A	0	A formal policy and procedures have not been developed or implemented. See 04-FAC1-6
FY 03	03-FAC6-8	The Finance And Administration Cabinet Should Develop And Apply Formal System Development Life Cycle Procedures For The Commonwealth's Cash And Investments Statistical Analysis System Programs	N/A	0	Follow up work performed for FY 2004 revealed that some improvements had been made, but also that there were still significant issues surrounding the program modification procedures. For FY 2004, the comment title has been changed to narrow the focus of the remaining issues. See 04-FAC4-9
FY 03	03-FAC7-9	The Office Of Financial Management Should Improve Segregation Of Duty Controls	N/A	0	Follow-up work performed for FY 2004 revealed that the there were still three main issues outstanding from FY 2003. These issues were split up and 3 formal comments were written. See 04-FAC5-10
FY 02	02-FAC3-6	The Finance And Administration Cabinet Should Develop And Consistently Apply Formal Change Management Control Procedures For The Commonwealth's Cash And Investment Statistical Analysis System Programs	N/A	0	See 04-FAC4-9
FY 02	02-FAC4-7	The Office Of Financial Management Should Improve Segregation Of Duty Controls	N/A	0	See 04-FAC5-10

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions (Continued):</u>					
<i>(2) Audit findings not corrected or partially corrected:</i>					
FY 01	01-FAC3-4	The Office Of Financial Management Should Improve Control Procedures Over Modifications To System Programs	N/A	0	See 04-FAC4-9
FY 00	00-FAC-6	The Office Of Financial Management Should Improve Control Procedures Over Modifications To System Programs	N/A	0	See 04-FAC4-9
FY 03	03-JUST1-32	The Justice Cabinet Should Either Develop An Indirect Cost Allocation Plan And Submit It To The Cognizant Federal Agency For Approval Or Stop Charging Indirect Costs To The Federal Government	16.575 16.579 16.588	\$46,774	Partially Resolved. Justice Cabinet submitted an indirect cost plan on Jan 31, 2005 to cognizant, but no indirect cost plan in place for FY 2004. See 04-JUST1-37.
FY 03	03-JUST2-33	The Justice Cabinet Should Follow Established Subrecipient Monitoring Policies And Procedures To Ensure Subrecipient Monitoring Is Properly Performed And Documented	16.575 16.579 16.588	0	Not Resolved. Exceptions noted during FY 04 testing. See 04-JUST2-38
FY 02	02-JUST2-40	The Justice Cabinet Should Develop Written Subrecipient Monitoring Policies and Procedures to Ensure Subrecipient Monitoring Is Properly Performed And Documented	16.575 16.579 16.588	0	Partially Resolved. Subrecipient monitoring procedures improved, but exceptions noted during FY 04 testing indicate that policies and procedures were not consistently followed. See 04-JUST2-38.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions (Continued):</u>					
<i>(2) Audit findings not corrected or partially corrected:</i>					
FY 03	03-MIL2-37	The Department Of Military Affairs Should Implement A System To Properly Monitor Subrecipient Activities To Comply With OMB Circular A-133 Compliance Requirements	97.036	0	Military Affairs developed extensive procedures which, if implemented, would expedite compliance. However, these policies were not implemented until January 2005. See 04-DMA5-49.
FY 02	02-MIL1-43	The Department Of Military Affairs Should Ensure Subrecipient Monitoring Is Properly Performed	97.036	0	See 04-DMA5-49.
FY 01	01-MIL1-46	The Department Of Military Affairs Should Ensure Subrecipients Meet OMB Circular A-133 Audit Requirements	97.036	0	See 04-DMA5-49.
FY 97	97-Military Affairs-50	The Department Of Military Affairs Should Strengthen Procedures For Monitoring Subrecipients	97.036	\$62,500	See 04-DMA5-49.
FY 00				(34,747)	
FY 02				(27,743)	
				<u>\$0</u>	
FY03	03-TC3-20	The Transportation Cabinet Should Implement Procedures To Ensure An Accurate Conversion of Data To New Systems	N/A	0	Corrective Action will not be implemented until the end of FY 04. See 04-TC2-14
FY03	03-TC4-21	The Transportation Cabinet Should Implement Procedures To Ensure The Integrity Of The Highway Information System Database	N/A	0	Corrective Action will not be implemented until the end of FY 04. See 04-TC3-15
FY03	03-TC5-22	The Transportation Cabinet Should Improve Data Retention Practices	N/A	0	Corrective Action will not be implemented until the end of FY 04. See 04-TC4-16

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions (Continued):</u>					
<i>(2) Audit findings not corrected or partially corrected:</i>					
FY03	03-TC6-23	The Transportation Cabinet Should Improve Audit Trail Procedures For Database Actions	N/A	0	Corrective Action will not be implemented until the end of FY 04. See 04-TC5-17
FY03	03-TC12-39	The Transportation Cabinet Should Maintain Documentation That Supports Figures Reported In the Annual Federal Highway Administration Statistics Report	N/A	0	See 04-TC11-45
FY02	02-TC2-46	The Transportation Cabinet Should Develop Internal Controls To Ensure Accurate Presentation Of the Annual Federal Highway Administration Statistics Report	20.205	0	See 04-TC11-45
FY02	02-TC3-47	The Transportation Cabinet Should Ensure The Annual Federal Highway Administration Report is Compiled In Compliance With Federal Guidelines	20.205	0	See 04-TC11-45
FY 03	03-CWD2-26	The Division Of Unemployment Insurance Should Enhance Controls To Ensure Proper Reporting Of The Closing Package	NA	0	See 04-CWD1-3.

(4) Audit finding is no longer valid or does not warrant further action:

No findings for this section.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Material Weaknesses/Noncompliances</u>					
<i>(1) Audit findings that have been fully corrected:</i>					
FY 02	02-REV3-31	The Kentucky Revenue Cabinet Should Have A System In Place To Reconcile Critical Information	N/A	0	Resolved during FY 04.
<i>(2) Audit findings not corrected or partially corrected:</i>					
FY 02	02-CWD2-32	The Division Of Unemployment Insurance Should Have A Computer System In Place To Adequately Maintain Employer Accounts	NA	0	Due to improvements, this finding was downgraded to a reportable condition in FY 03. See 04-CWD1-3.
<i>(3) Corrective action taken is significantly different from corrective action previously reported:</i>					
No findings for this section.					
<i>(4) Audit finding is no longer valid or does not warrant further action:</i>					
No findings for this section.					

APPENDICES

**COMMONWEALTH OF KENTUCKY
APPENDIX 1
FOR THE YEAR ENDED JUNE 30, 2004**

List Of State Organizations Audited As Part Of The
Statewide Single Audit Of The Commonwealth

The list includes agencies receiving only financial statement audits used for preparing the Commonwealth's CAFR. CPA reports are available upon request to the respective audited agency.

**STATE ORGANIZATIONS AUDITED BY CERTIFIED PUBLIC ACCOUNTING
FIRMS AND INCLUDED IN SSWAK:**

Kentucky Affordable Prepaid Tuition
Kentucky Center for the Arts
Bluegrass State Skills Corporation
Eastern Kentucky Exposition Center Corporation
Kentucky Economic Development Finance Authority
Kentucky Educational Savings Plan Trust
Kentucky Educational Television Authority
Kentucky Higher Education Assistance Authority
Kentucky Higher Education Student Loan Corporation
Kentucky Horse Park
Kentucky Housing Corporation
Kentucky Infrastructure Authority
Judicial Form Retirement System
Kentucky Local Correctional Facilities Construction Authority
Kentucky Lottery Corporation
Office of the Petroleum Storage Tank Environmental Assurance Fund
Council on Postsecondary Education
Kentucky Public Employees' Deferred Compensation Authority
Kentucky Retirement Systems
Kentucky River Authority
Kentucky State Fair Board
Kentucky Teachers' Retirement Systems
Turnpike Authority of Kentucky
Kentucky Worker's Compensation Funding Commission
Kentucky Worker's Compensation Special Fund, Coal Workers' Pneumoconiosis Fund
(functions of the Labor Cabinet), and Uninsured Employers' Fund (function of the Office
of the Attorney General)

**COMMONWEALTH OF KENTUCKY
APPENDIX 1
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

List Of State Organizations Audited As Part Of The Statewide Single Audit Of The Commonwealth (Continued)

STATE ORGANIZATIONS AUDITED BY CERTIFIED PUBLIC ACCOUNTING FIRMS AND NOT INCLUDED IN SSWAK, EXCEPT FOR EXPENDITURE AMOUNTS IN THE OPINION LETTER:

Eastern Kentucky University
Kentucky Community Technical College System
Kentucky State University
Morehead State University
Murray State University
Northern Kentucky University
University of Kentucky
University of Louisville
Western Kentucky University

STATE ORGANIZATIONS AUDITED BY THE AUDITOR OF PUBLIC ACCOUNTS:

Kentucky Access Program (Financial Statements Only)
Berea Artisans Center (Financial Statements Only)
Cabinet for Families and Children
Cabinet for Health Services
Cabinet for Workforce Development
Department of Education
Department of Fish and Wildlife Resources (Federal Awards Only)
Department of Labor (Federal Awards Only)
Department of Military Affairs (Federal Awards Only)
Department of Parks (Financial Statements Only)
Department of Revenue
Department of Veterans Affairs (Federal Awards Only)
Finance and Administration Cabinet
Justice Cabinet (Federal Awards Only)
Natural Resources and Environmental Protection Cabinet (Federal Awards Only)
Office of the Kentucky State Treasurer - Cash Functions
Transportation Cabinet

**COMMONWEALTH OF KENTUCKY
APPENDIX 2
FOR THE YEAR ENDED JUNE 30, 2004**

List Of State Organization Contacts

If additional copies of the statewide single audit are required, please contact Gregory Giesler, Open Records Administrator, with the APA's office at (502) 573-0050 or gregory.giesler@auditor.ky.gov. If copies of the CAFR for the FY 04 are required, please contact Robbie Rudolph, Finance and Administration Cabinet Secretary, at (502) 564-4240.

The following is a list of individuals by state organizations to contact regarding findings in the Schedule of Findings and Questioned Costs or the Summary Schedule of Prior Audit Findings.

State Organization	Contact
Cabinet for Families and Children	Kelli Hill, Staff Assistant Division of Financial Management Office of Fiscal Services Cabinet for Families and Health Services 275 East Main Street 4C-C Frankfort, KY 40601 Phone (502) 564-2250 ext. 4336
Cabinet for Health Services	Miles Murphy, Assistant Director Division of Policy and Financial Management Cabinet for Families and Health Services 275 East Main Street 4E-A Frankfort, KY 40601 Phone (502) 564-8890 Ext. 3374
Cabinet for Workforce Development	Tommy Goins, Branch Manager Division of Fiscal Services Cabinet of Workforce Development 500 Mero Street 9th Floor Frankfort, KY 40601 Phone (502) 564-3300
Department of Fish and Wildlife Resources	Sherry Kefauver, Internal Policy Analyst Department of Fish & Wildlife Resources #1 Game Farm Road Frankfort, KY 40601 Phone (502) 564-7109

**COMMONWEALTH OF KENTUCKY
APPENDIX 2
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

List Of State Organization Contacts (Continued)

Department of Military Affairs	Rick Flynn, Chief Administrative Officer Division of Administrative Services Department of Military Affairs Boone National Guard Center 100 Minuteman Parkway, EOC Building Frankfort, KY 40601 Phone (502) 607-1545
Department of Parks	Robert Richards, Director Division of Financial Operations Department of Parks Commerce Cabinet 500 Mero Street, 11 th Floor Frankfort, KY 40601 Phone (502) 564-2172
Department of Revenue	Eddie Mattingly, Division Director Kentucky Department of Revenue 200 Fair Oaks Lane, Station 1 Frankfort, KY 40620 Phone (502) 564-3226
Department of Veterans Affairs	David Worley, Branch Manager Kentucky Veterans Cemeteries Department of Veterans Affairs 1111 Louisville Road Frankfort, KY 40601 Phone (502) 564-9281
Finance and Administration Cabinet	Stuart Weatherford, Director Division of Statewide Accounting Services Finance and Administration Cabinet Capitol Annex, Room 484 702 Capitol Avenue Frankfort, KY 40601 Phone (502) 564-7750

**COMMONWEALTH OF KENTUCKY
APPENDIX 2
FOR THE YEAR ENDED JUNE 30, 2004
(CONTINUED)**

List Of State Organization Contacts (Continued)

State Organization	Contact
Finance and Administration Cabinet (Continued)	Ed Ross, Controller Office of the Controller Finance and Administration Cabinet Capitol Annex, Room 393 702 Capitol Avenue Frankfort, KY 40601 Phone (502) 564-2210 Tom Howard, Acting Executive Director Office of Financial Management Finance and Administration Cabinet Capitol Annex, Room 261 702 Capitol Avenue Frankfort, KY 40601 Phone (502) 564-2924
Justice Cabinet-Office of the Secretary	Tanya Dickinson, Branch Manager Division of Grants Management Justice Cabinet 403 Wapping St Frankfort, KY 40601 Phone (502) 564-3251
Natural Resources and Environmental Protection Cabinet	Lisa Cox, Director Division for Administrative Services Natural Resources and Environmental Protection Cabinet 500 Mero Street, 4 th Floor Frankfort, KY 40601 Phone (502) 564-7364
Transportation Cabinet	Debra Gabbard, Executive Director Office of Policy & Budget Transportation Cabinet 200 Mero Street Frankfort, KY 40601 Phone (502) 564-4550